

1                   THE UNITED STATES DISTRICT COURT  
2                   FOR THE MIDDLE DISTRICT OF NORTH CAROLINA

3       RICHARD G. TATUM, individually   Civil action  
4       and on behalf of a class of       No.   1:02CV373  
5       all other persons similarly  
6       situated,  
7               Plaintiffs,

8       vs.                               Greensboro, North Carolina  
9                                       February 2, 2010

10       R.J. REYNOLDS TOBACCO COMPANY,  
11       et al,  
12               Defendants.

13       -----/

14                               VOLUME XV

15                   TRANSCRIPT OF BENCH TRIAL PROCEEDINGS  
16                   BEFORE THE HONORABLE N. CARLTON TILLEY, JR.

17                   UNITED STATES DISTRICT JUDGE

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36       Transcript produced by computer-aided transcription.

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<u>WITNESSES FOR THE</u> <u>DEFENSE:</u>				
John Montgomery	8			

1           THEREUPON, the following proceedings were had:)

2           THE COURT: It is good to be on the other side of  
3 a closed door coming into a courtroom and hear the attorneys  
4 laughing. It's a good sign.

5           Mr. Charnes, are you ready?

6           MR. CHARNES: We are ready to call John  
7 Montgomery.

8           MR. LEWIS: Before we start, may I raise an issue?  
9 We have just received, several minutes ago, a stack of brand  
10 new exhibits that we've never seen before. These are not  
11 documents that were attached to Mr. Montgomery's report or  
12 supplemental report. They may be new opinions. I mean,  
13 they are detailed charts and tables, so I guess to the  
14 extent anything other than illustrative, fairly  
15 illustrative, we don't know that, past opinions in his  
16 report we would object to them being used. I'm not quite  
17 sure how to take it up procedurally. Obviously we've not  
18 had time to analyze this.

19           THE COURT: Why don't we take a recess and you can  
20 look at them. If the Defense wishes to present those during  
21 Mr. Montgomery's testimony, then you may explain to the  
22 Plaintiff what they are, and then with everybody having some  
23 information about them, we'll come back and talk about  
24 whether they would be appropriate or not.

25           MR. LEWIS: We did get a very brief explaining,

1 but didn't have time before Your Honor came to the bench, so  
2 I think it would probably be helpful.

3 THE COURT: You let us know when you are ready or  
4 have reached an impasse that needs the Court's presence.

5 MR. LEWIS: Thank you, Your Honor.

6 (Recess taken.)

7 THE COURT: Where are we?

8 MR. LEWIS: Your Honor, we are satisfied that as  
9 far as the new exhibits, with one exception, they are  
10 extracted from or somehow relate to things in the witness's  
11 reports. We're going to have -- this is a summary, a set of  
12 opinions as we saw with Mr. Raborn, one of which we don't  
13 believe is contained in the report, so we have a  
14 disagreement about that.

15 I don't know when the best time to take that up  
16 is. I'll leave that to Your Honor's discretion.

17 THE COURT: Do you want to go ahead and do that  
18 now?

19 MR. LEWIS: And specifically, we're looking at  
20 opinion one on Defendant's Exhibit 239, and although  
21 Mr. Montgomery in his reports, to be fair about it, does  
22 say -- have certain portions of his reports where he says  
23 there was no reason to expect what he calls extraordinary  
24 returns from NGH and NA, but no where in his reports is  
25 there any comparison of what can be achieved from the

1 Diversified Investment Fund. Those words don't appear  
2 anywhere in the report.

3 Mr. Charnes has pointed me to one paragraph in  
4 Doctor Montgomery's supplemental report, which is Paragraph  
5 4, and it is Defense Exhibit 64.

6 THE COURT: What page?

7 MR. LEWIS: Page 2 of the report.

8 THE COURT: That's Paragraph 4?

9 MR. LEWIS: That's correct, Your Honor.

10 THE COURT: Let me take a moment to read this  
11 then.

12 Do you wish to be heard at more length, Mr. Lewis?

13 MR. LEWIS: I think the words speak for  
14 themselves, Your Honor. So pending hearing from opposing  
15 counsel --

16 MR. CHARNES: I think Mr. Lewis is quibbling with  
17 the language here. That sentence in Page 2 and Paragraph 4  
18 indicates that was the whole point of his original report,  
19 and much of the supplemental report -- there was no reason  
20 to expect, as it says there, the Nabisco Stock delivered  
21 extraordinary returns.

22 Extraordinary returns, Doctor Montgomery will  
23 testify by definition means, a return greater than you could  
24 achieve from a diversified portfolio of stocks. So it's  
25 using different language, but the concept is exactly the

1 same, but I think it's clear from the context of Doctor  
2 Montgomery's report and testimony, that it's talking about  
3 exactly the same thing.

4           Extraordinary returns is -- Doctor Montgomery's  
5 use of the term extraordinary return is the same, I think,  
6 as Professor Lys has used the phrase abnormal returns, that  
7 means a return greater than you could get in the stock  
8 market as a whole, or diversified set of stocks that  
9 achieve -- that diversify away the company's specific risk.

10           So I think the concept that he's expressing in his  
11 reports and as are summarized in that sentence on Page 2, is  
12 exactly what he is crystallizing in opinion one. I think it  
13 is the same point, as will be clear during his testimony.

14           THE COURT: Opinion one or opinion three?

15           MR. CHARNES: Opinion one is the one I think  
16 Mr. Lewis is objecting to.

17           THE COURT: I understood it was opinion three.

18           MR. LEWIS: No. Opinion one, Your Honor.

19           THE COURT: And that may be saying the same thing  
20 in different words. Why don't we allow him to testify. You  
21 may cross-examine him, and if at the conclusion of the  
22 testimony it appears that it is an opinion which has not  
23 reasonably been stated in his report or supplemental report,  
24 then let's address where we go from there.

25           MR. LEWIS: Thank you, Your Honor.

1 THE COURT: Sure.

2 MR. CHARNES: Your Honor, for at least the initial  
3 sections of the initial part of Doctor Montgomery's  
4 testimony, we'll be using defense binders two and four.

5 THE COURT: Okay.

6 (JOHN D. MONTGOMERY, DEFENSE WITNESS, WAS  
7 SWORN.)

8 DIRECT EXAMINATION

9 BY MR. CHARNES:

10 Q. Good morning, Doctor Montgomery.

11 A. Good morning.

12 Q. Would you please state your name for the record.

13 A. John Dennison Montgomery.

14 Q. Doctor Montgomery, do you have a Ph.D in economics?

15 A. Yes, I do. From Princeton University.

16 Q. And what year did you receive that Ph.D.?

17 A. 1990.

18 Q. Would you please describe for the Court the remainder  
19 of your educational background.

20 A. Yes. Starting from the beginning, I have a bachelor of  
21 arts from Yale University. My major was economics. I have  
22 a masters of science from the London School of Economics,  
23 that was 1985. I should say also my BA was in 1982. Then I  
24 have my Ph.D. from Princeton.

25 Q. And, Doctor Montgomery, who is your present employer?



1 A. I'm presently employed by NERA, N-E-R-A Economic  
2 Consulting.

3 Q. Is NERA an acronym?

4 A. It is. It used to be -- the name of the firm used to  
5 be National Economic Research Associates. So in some sense,  
6 NERA is an acronym for that.

7 Q. What is NERA Economic Consulting?

8 A. NERA is a firm of economists, mathematicians,  
9 accountants and other professionals providing analytical  
10 services in consulting and other areas for governments,  
11 regulators, businesses, corporations, parties in litigation.

12 Q. And approximately how many professionals does NERA  
13 Economic Consulting employ?

14 A. Worldwide, it's about 500.

15 Q. And what is your current position at NERA?

16 A. I'm a senior vice president.

17 Q. How long have you held that position?

18 A. A couple weeks now. I was promoted recently.

19 Q. Congratulations.

20 A. Thank you.

21 Q. What are your job responsibilities as senior vice  
22 president?

23 A. My responsibility is to direct projects in --  
24 consulting projects and expert testimony projects in finance  
25 and securities areas.

1 Q. And what was your position before you were promoted to  
2 senior vice president?

3 A. I was a vice president.

4 Q. And when did you begin as vice president?

5 A. In 2006.

6 Q. And before 2006 when you were a vice president, what  
7 was your position?

8 A. Title was called senior consultant. In all of these  
9 positions my duties have essentially been the same over  
10 time.

11 Q. And what year did you become a senior consultant with  
12 NERA?

13 A. When I joined the firm in 2002.

14 Q. In the position as senior consultant, vice president  
15 and senior vice president, do you supervise other employees  
16 of NERA?

17 A. Yes, I do. Ranging from three or four, up to eight,  
18 possibly depending on the nature of the project that I'm  
19 involved in.

20 Q. And during your entire employment with NERA, have you  
21 provided consulting advice on securities and finance  
22 matters?

23 A. Yes. That's been the bulk of my focus.

24 Q. During your employment with NERA, have you worked on  
25 matters involving ERISA and ERISA plans?

1 A. Yes, I have. I've worked on approximately -- somewhere  
2 between 15 and 20 projects related to ERISA issues during my  
3 employment at NERA.

4 Q. And at NERA do you provide any nonlitigation consulting  
5 services?

6 A. I provide some. I've been involved in some advising of  
7 companies involved in transactions.

8 Q. And in your personal work at NERA, have you represented  
9 any governmental entities?

10 A. I have served as a consultant to governmental entities.  
11 I've been a consultant to the U.S. Attorneys Office for the  
12 and Southern District of New York in a criminal insider  
13 trading case. I've also been a consultant to the Ontario  
14 Security Commission in Canada, also on an insider trading  
15 case.

16 Q. Prior to joining NERA in 2002, by whom were you  
17 employed?

18 A. Immediately before my employment at NERA, I was vice  
19 president and senior economist at Morgan Stanley in New  
20 York, which is investment bank.

21 Q. What years were you employed by Morgan Stanley?

22 A. 1998 through 2001.

23 Q. What were your job responsibilities at Morgan Stanley?

24 A. My responsibilities were to cover global economic  
25 developments and developments in global financial markets,

1 and to develop currency, equity and bond markets and to  
2 write those views about the economics and finance, to  
3 provide that information to the firm's clients.

4 Q. Who were Morgan Stanley's clients that received your  
5 opinion?

6 A. It was a big distribution system, so I don't think I  
7 know all of them. They were institutional investors, hedge  
8 funds, investment advisors, consultants.

9 Q. With whom were you employed prior to joining Morgan  
10 Stanley in 1998?

11 A. Immediately prior to that, I was an economist in the  
12 capital markets and financial studies division of the  
13 International Monetary Fund in Washington, DC.

14 Q. What years were you employed there?

15 A. Overall, 1993 to 1998. I did spend one year on a leave  
16 of absence from the IMF, as a senior staff economist on the  
17 President's Council of Economic Advisors.

18 Q. Before we get to that, can you just please describe for  
19 the record what the International Monetary Fund is.

20 A. The International Monetary Fund is an international  
21 organization that the United States and most other countries  
22 are members of. It was organized by a treaty immediately  
23 following World War II, and its primary functions are to  
24 provide surveillance of member countries' economic and  
25 financial policies, to identify potential risks, and to

1 provide lending to countries having balance of payments and  
2 financial difficulties.

3 Q. What were your responsibilities as an economist at the  
4 International Monetary Fund?

5 A. I was part of a group that monitored, evaluated and  
6 wrote on financial systems and financial issues in countries  
7 that were considered important to the international  
8 financial and economic system.

9 Q. You mentioned that you were -- during the period -- at  
10 some point between 1993 and 1998 you were also employed by  
11 the President's Council as an economic advisor?

12 A. Yes. I was a senior staff economist in charge of  
13 international issues from mid 1996 to mid 1997. I provided  
14 briefings to the president, and I worked a wide range of  
15 policy issues as a representative for the Council of  
16 Economic Advisors on interagency policy issues and finance  
17 and trade issues. I was one of about ten senior staff  
18 economists on the council.

19 Q. Can you please describe for the record what the  
20 President's Council for Economic Advisors is?

21 A. It is a council. It is a small group within the  
22 executive office of the President, charged with providing  
23 economic advice to the President in his or her policy making  
24 role.

25 Q. Doctor Montgomery, how were you employed before

1 beginning work with the International Monetary Fund in 1993?

2 A. I was an economist at the Board of Governors of the  
3 Federal Reserve System in Washington from 1989 when I left  
4 graduate school, to 1993.

5 Q. And what is the Board of Governors of the Federal  
6 Reserve?

7 A. It is the central governing organization, and  
8 analytical organization for the Federal Reserve system,  
9 which is a system of 12 banks which make up Federal Reserve  
10 banks, which make up the nation's central bank.

11 Q. What were your responsibilities as an economist with  
12 the Federal Reserve?

13 A. I was in charge of working on a variety of financial  
14 issues, primarily international financial issues and banking  
15 issues. I also provided economic analysis for a foreign  
16 country, France, part of that time.

17 Q. Now, did you testify that your position at the Federal  
18 Reserve was the first job you held after receiving your  
19 Ph.D?

20 A. Yes, I did.

21 Q. And before you received your Ph.D., did you have any  
22 full time employment?

23 A. I did. For most of the time between college and  
24 getting my Ph.D. I was a securities analyst at the  
25 brokerage firm of J. Bush and Company in New York City.

1 Q. And during what years were you employed by J. Bush and  
2 Company?

3 A. 1982 to 1984.

4 Q. What were your responsibilities as a securities analyst  
5 at J. Bush and Company?

6 A. I analyzed the finances and business trends for  
7 companies in a variety of industries. I prepared reports.  
8 I forecasted earnings, and I discussed the companies that  
9 are covered with our institutional plans.

10 Q. What was included in the reports that you drafted as  
11 an employee of J. Bush and Company?

12 A. They included, as best I can recall, discussion of the  
13 prospects of the company, the nature of the business, the  
14 trends in different parts of the company's business, and the  
15 finances of the companies. They included projections for  
16 earnings.

17 Q. And what kind of companies did you research and write  
18 reports about when you were employed with J. Bush and  
19 Company?

20 A. Most of them were relatively small companies. They  
21 were in a range of industries. They include banks,  
22 companies in the defense industries. I think there was a  
23 toy company. There were others. Pharmaceutical companies.

24 Q. Doctor Montgomery, I would like you to turn to  
25 Defendant's Exhibit 238. What is Defendant's Exhibit 238?

1 A. This is a copy of my curriculum vitae that was attached  
2 to my initial expert report in this case.

3 Q. If you would please review the first page of DX 238, I  
4 would like to ask you whether this page accurately  
5 summarizes your educational and work experience about which  
6 you just testified.

7 A. It does, with the exception that it doesn't reflect my  
8 current title at NERA.

9 Q. Which is senior vice president?

10 A. That's correct.

11 Q. If you would please review pages two and three of  
12 Defendant's Exhibit 238, and I would like to ask you if  
13 these pages accurately reflect the publications that you  
14 have authored and coauthored.

15 A. Yes, they do. The one exception is, that since I  
16 drafted this list of publications, I had an additional  
17 publication published on NERA's website as a working paper.  
18 That publication discussed the financial policies by the US  
19 Government and Federal Reserve, related to the recent  
20 financial crisis.

21 Q. And are the publications listed on pages two and three  
22 in the areas of finance and securities?

23 A. Yes. They all are. Well, let me -- that is true with  
24 one partial exception, and that is the chapter of the  
25 economic -- on page three which deals with financial issues



1 and other economic issues, but everything else has to do  
2 with finance and securities.

3 Q. Could you please turn to page three of your CV. Does  
4 this page accurately reflect your professional affiliations?

5 A. Yes, it does.

6 Q. You are a member of the American Economic Association?

7 A. Yes. I am a member of the American Economic  
8 Association.

9 Q. What is the American Economic Association?

10 A. The AEA is an organization of professional economists,  
11 mostly academic economists. It is the preeminent  
12 association of academic economists in the United States.

13 Q. You are also a member of the American Finance  
14 Association?

15 A. That is a similar organization to the American Economic  
16 Association for professionals in financial academics as well  
17 as practicing financial specialists.

18 Q. Doctor Montgomery, have you testified as an expert  
19 witness in other cases?

20 A. Yes, I have.

21 Q. If you please turn to page two of your CV. Does page  
22 two accurately list your expert testimony?

23 A. Yes, it does.

24 Q. Doctor Montgomery, have you been paid directly by the  
25 Defendant for your work in this case?

1 A. No. I work for NERA. NERA bills RJR.

2 Q. So you're --

3 A. So I'm not paid directly, no.

4 Q. So NERA has been compensated for the work of you and  
5 others at the firm in this case?

6 A. That's correct.

7 Q. What is your hourly rate?

8 A. My hourly rate for working this case is 465 an hour.

9 Q. And what is the range of hourly rates of the other NERA  
10 personnel who have assisted you in this case?

11 A. It ranges from about \$95 an hour for clerical staff, up  
12 to about 450-dollar an hour for some other senior staff.  
13 There is one exception. I believe there is one hour of  
14 billed time by somebody whose billing rate was about \$600 an  
15 hour.

16 Q. Has all of the work that NERA billed in this case been  
17 related to your expert testimony?

18 A. No. NERA has provided -- I have provided a variety of  
19 consulting and a variety of other issues related to this  
20 case, and I believe others at NERA have also.

21 Q. What is the total amount that NERA has billed to date  
22 with respect to your work and NERA's work in this case?

23 A. Including bills that haven't yet been sent, it's a  
24 little over two million dollars for all the work that NERA  
25 has done.

1 Q. Doctor Montgomery, do you have -- of the approximately  
2 \$2 million, do you have an estimate for the amount that was  
3 related directly to the preparation of your opinions in this  
4 case?

5 A. Focusing just on the work that was done around -- can't  
6 quite break it up by how much was done related to my  
7 opinions, but if I could go back and look at how much was  
8 done during the period in which I and my staff prepared my  
9 two expert reports and reviewed the expert reports from the  
10 other side, and there is a little bit of other work in that  
11 time, but all and all, the bills for that period were just  
12 about exactly a million dollars. About 450,000 of that  
13 related to programmers time, mostly involved in damages  
14 calculations, and I think a little bit more than \$200,000 of  
15 it related to my time.

16 Q. Do you know, Doctor Montgomery, for your personal time  
17 that you've billed in this case, how much have you -- strike  
18 that.

19 How much has NERA billed for your personal time in this  
20 case, from start to finish; if you know?

21 A. It's around \$500,000.

22 Q. Is the compensation that either you or NERA is  
23 receiving in any way dependent on the outcome of this case?

24 A. No, it's not.

25 Q. Doctor Montgomery, have you been retained by the

1 Defendants to offer an opinion in this case?

2 A. Yes, I have.

3 Q. Have you formed one or more opinions with regard to  
4 this case?

5 A. Yes, I have.

6 MR. CHARNES: Your Honor, we would tender Doctor  
7 Montgomery as an expert in the evaluation of securities,  
8 finance, economics, investing, the stock market, portfolio  
9 diversification, market efficiency and the computation of  
10 damages. I can repeat that.

11 THE COURT: Is that all?

12 MR. LEWIS: Could I have that read back, Your  
13 Honor? I didn't get them all.

14 THE COURT: Okay, Mr. Charnes.

15 MR. CHARNES: Valuation of securities, finance,  
16 economics, investing, the stock market, portfolio  
17 diversification, market efficiency, and the computation of  
18 damages.

19 MR. LEWIS: May we have a moment?

20 THE COURT: Sure.

21 MR. LEWIS: We certainly don't quarrel with Doctor  
22 Montgomery's expertise in most of those areas; finance,  
23 economics, et cetera. There are three of them which I would  
24 like the opportunity to voir dire on.

25 THE COURT: You may proceed.

1 MR. LEWIS: Okay.

2 VOIR DIRE EXAMINATION

3 BY MR. LEWIS:

4 Q. Doctor Montgomery, good morning. As you know from your  
5 deposition, I'm Jeff Lewis, one of the attorneys for the  
6 Plaintiff.

7 A. Yes.

8 Q. Have you ever measured investment diversification for a  
9 client, other than in litigation?

10 A. Not that I can recall, no.

11 Q. Have you ever published an article on investment  
12 diversification?

13 A. Not specifically on that subject, no.

14 Q. Have you ever taught a class on investment  
15 diversification, or a course?

16 A. Well, I've taught at the assistant level at a  
17 university as part of my graduate studies on finance, and  
18 investment diversification is part of the general curriculum  
19 of finance.

20 Q. Have you ever spoken at a public program or association  
21 program with regard to investment diversification?

22 A. Not narrowly and specifically on that subject. I have  
23 spoken on general portfolio issues related to ERISA.

24 Q. Have you ever written any articles on the efficient  
25 market hypothesis?

1 A. No, I have not.

2 Q. Have you ever testified as an expert with regard to the  
3 efficient market hypothesis, other than in this case?

4 A. Other than in this case -- I would have to go back and  
5 look at my testimony record. May I do that?

6 Q. Certainly.

7 A. I'm forgetting the exhibit number.

8 Q. If you are referring to your CV, it is Defendant's  
9 Exhibit 238.

10 A. Let me -- I just want to make sure. I don't know the  
11 answer to that question. No. I have not. I have not  
12 testified on that subject, although it's, I think, been a  
13 presumption behind some of the other work that I've done.

14 Q. Have you ever authored any publication on the  
15 investment of assets?

16 A. Well, a lot of the work I did at Morgan Stanley as well  
17 as with J. Bush, involved providing advice of various sorts  
18 on the investments of assets. The work I did at the  
19 International Monetary Fund involved reviews of various  
20 issues having to do with financial markets and an important  
21 part of that has to do with investment, with the investment  
22 of assets.

23 My Ph.D dissertation had to do with the international  
24 capital, which also involved money flowing from the sources  
25 of those, and savings to uses of the savings, that is

1 investments, so I think I have written on the investment of  
2 assets and those types of things.

3 Q. Did you testify at your deposition that other than your  
4 work at Morgan Stanley -- did you testify at your deposition  
5 that you did not offer any document on investment of assets  
6 specifically?

7 A. I don't recall. I don't remember if I did.

8 THE COURT: You don't remember if you testified?

9 THE WITNESS: I don't remember if I testified,  
10 yes.

11 BY MR. LEWIS:

12 Q. Doctor Montgomery, do you recall having your deposition  
13 taken in this case?

14 A. Yes, I do.

15 Q. I've handed you the original transcript of your  
16 deposition. Does that look like -- in fact, have you had an  
17 opportunity to review the transcript of your deposition  
18 since it was taken?

19 A. Yes, I have.

20 Q. And is this a copy of that transcript?

21 A. Yes. Just flipping through, it appears to be.

22 Q. Can I direct your attention, please, to Page 138, and  
23 direct your attention to Line 15, and I'm going to read the  
24 question, and I would ask you to read the answer, please,  
25 and we're just going to read from there, on the line that

1 says, discussion off the record, all the way to 139, Line 9.

2 "Question: And have you authored or coauthored any  
3 publications on investment of assets?"

4 A. I'm sorry, you want me to read the answer?

5 Q. Please.

6 A. "Answer: I think it depends on how you look at what  
7 I've -- what I've written. Much of the work that I've done  
8 at Morgan Stanley involves providing advice on the  
9 allocation of investments, and I'm not -- I don't believe  
10 I've done any other work that's related to that issue."

11 Q. Actually, we'll stop there in that deposition  
12 testimony.

13 You've mentioned allocation of assets. Did that  
14 include -- did you publish any articles on investment -- on  
15 individual securities investment decisions?

16 Let me rephrase that. Have you ever published any  
17 article on the issue of decision-making as to individual  
18 securities?

19 A. Not that I can recall, with the exception of the  
20 analyst reports that I wrote at J. Bush and Company.

21 Q. That was 1982 through 1984?

22 A. Correct.

23 Q. Leaving aside your graduate school teaching duties,  
24 have you ever taught any course on investments and  
25 securities?



1 A. No. I don't believe I have.

2 Q. Do you claim to be an expert on what individual  
3 investors specifically do?

4 A. I claim to be an expert on the lessons to be taken from  
5 the study of financial economics for what individual  
6 investors do. I don't claim to be an expert on other  
7 aspects of what individual investors do.

8 Q. Do you claim to be an expert on the practices of  
9 knowledgeable experienced investors?

10 A. I think I would give the same answer. I believe I'm an  
11 expert on what the study of financial economics has learned  
12 about the practices of investors, but more broadly, I don't  
13 claim to be an expert.

14 Q. Other than with regard to your work at J. Bush and  
15 Company from 1982 to 1984, did you ever advise a client with  
16 regard to buying and selling an individual stock?

17 A. No, I don't believe I have.

18 Q. Do you claim to be an expert on the analysis of  
19 securities?

20 A. I believe that a large part of that is related to my  
21 expertise in financial economics, so again, I believe that  
22 my expertise in financial economics extends to a large  
23 portion of the analysis of securities. I believe I would  
24 say in part, but not in general.

25 Q. Is it fair to say that you have never published any

1 research that bears on the analysis of an individual  
2 security?

3 A. Again, with the exception of the analysis that I did on  
4 individual securities in my first job, that's correct.

5 Q. Those were -- the publications were internal to your  
6 clients, is that correct? Those publications that you did  
7 at J. Bush and Company, were they publications you authored  
8 at the J. Bush and Company disseminated to anybody other  
9 than internally and clients?

10 A. I don't know for sure. Not that I know of, no. They  
11 were not made available to the general public. We never  
12 sold on the newsstand or anything like that.

13 Q. These articles were not submitted to journals?

14 A. No.

15 Q. They were not peer reviewed?

16 A. No, they were not.

17 Q. Have you ever published any articles that address the  
18 topic of analyst reports?

19 A. No, I have not.

20 Q. And for purposes of this case, have you ever done any  
21 empirical research into analyst reports or recommendations?

22 A. No, I have not.

23 Q. Before your assignment in this case, did you ever at  
24 any time engage in a review of published literature  
25 regarding the usefulness of analyst reports and

1 recommendations?

2 A. Could you repeat that?

3 Q. Before your engagement in this case, did you ever make  
4 any systematic study of the literature regarding analyst  
5 recommendations?

6 A. Well, first of all, I don't think there is that much  
7 literature like that. But, no, I did not make a systematic  
8 study.

9 MR. LEWIS: One moment, Your Honor.

10 THE COURT: Surely.

11 BY MR. LEWIS:

12 Q. Doctor Montgomery, in your -- in an exhibit to your  
13 report in this case, did you list certain articles that you  
14 had reviewed in the course of preparing that report?

15 A. Yes, I did. I think there is probably a list in both  
16 my supplemental and my original report.

17 Q. In the list attached to your original report, did you  
18 include some articles related to analyst reports and  
19 recommendations?

20 A. I believe I did.

21 Q. Had you ever read any of those articles prior to  
22 becoming involved in this case?

23 A. I don't know.

24 Q. Would you like to look at the list?

25 A. If you want.

1 THE COURT: Yes, please.

2 MR. LEWIS: Your Honor, can we direct -- I'll get  
3 Plaintiff's Exhibit 397.

4 BY MR. LEWIS:

5 Q. Let me direct your attention to Plaintiff's Exhibit  
6 397, specifically to Exhibit 2, which is on -- the pages are  
7 not Bates stamped, Your Honor, so we can't direct you to it.  
8 There are about 35 pages to the report, and then there is an  
9 Exhibit 1, which has four -- three pages and --

10 A. It is a bit less than half-way.

11 Q. I want to direct your attention, when you get there, to  
12 Page 4 of 7 and Page 5 of 7, and ask for you to review the  
13 academic articles that appear on Page 4.

14 Does that refresh your memory as to whether -- strike  
15 that.

16 Would you agree that that article number 89, it's on  
17 Page 5 -- 95, 96, are all related to the analyst  
18 recommendations and reports?

19 A. Yes, they are.

20 Q. Having reviewed this list, does that refresh your  
21 memory as to whether or not prior to your engagement in this  
22 case, you had ever reviewed any of those articles?

23 A. No. I am actually not sure whether I looked at these  
24 before. I mean, I generally keep up on the literature on  
25 financial economics. I look at journals when they come out.

1 It's hard for me to recall. I mean, I see many articles.

2 It's hard for me to recall.

3 Q. But as you sit here today, you can't tell us, can you,  
4 that you ever read -- that you had ever read any of those  
5 articles before your engagement in this case?

6 A. No, I can't tell you I have.

7 Q. Do you have any experience administering a 401(K) plan?

8 A. No, I don't.

9 Q. Have you ever provided consulting services with regard  
10 to the operation or administration of a 401(K) plan?

11 A. Not with regard to the operation or administration, no.

12 Q. Before issuing your report in this case, or reports in  
13 this case, had you ever addressed in any way the issue of  
14 how 401(K) plan participants make or do not make investment  
15 decisions?

16 A. I believe I have dealt with that issue in other  
17 litigation projects that I've worked on.

18 MR. LEWIS: If I could have one moment, Your  
19 Honor.

20 THE COURT: You may.

21 MR. LEWIS: Your Honor, I have no further  
22 questions, and if Your Honor would like to hear argument  
23 about what the witness is not an expert in.

24 THE COURT: I'm going to give Mr. Charnes an  
25 opportunity to follow up on your questions.

1 BY MR. CHARNES:

2 Q. Thank you, Your Honor. Doctor Montgomery, in your  
3 academic training, your Ph.D., did you receive course work  
4 regarding investment diversification?

5 A. I received extensive course work in financial  
6 economics, which includes as a very basic of that, the  
7 theory of investment diversification.

8 Q. During that academic training, did you also receive  
9 course work on efficient market hypothesis?

10 A. Again, that's part of the basic theory of finances  
11 taught at the Ph.D. level.

12 Q. Is the same thing true with investments and securities?

13 A. It's part of the same theory, yes.

14 Q. Is it fair to say that in order to receive a Ph.D. in  
15 finance and economics, you have to show a level of  
16 proficiency in those areas, that is investment  
17 diversification, efficient market hypothesis and investments  
18 and evaluation of securities?

19 A. Yes.

20 Q. In the course of -- strike that.

21 Are you familiar with the literature published in the  
22 fields of finance?

23 A. Yes, I am.

24 Q. Did you just testify that you keep current with that  
25 literature on a regular basis as part of your being an

1 economist?

2 A. Yes, I do.

3 Q. Apart from this case, or work in this case, you keep  
4 current with that?

5 A. Yes.

6 Q. And you engage in discussions at NERA and outside of  
7 NERA with other economists about matters related to finance  
8 and the like?

9 A. Yes, I am.

10 Q. Have you reviewed this literature as indicated in your  
11 original report in connection with the formation of your  
12 opinions in this case?

13 A. I'm sorry, I reviewed what literature?

14 Q. Academic literature related to -- I'll take them one by  
15 one.

16 Have you reviewed the academic literature related to  
17 analyst reports in forming your opinions in this case?

18 A. Yes.

19 MR. LEWIS: Could I object to the form of the  
20 question, ambiguous.

21 THE COURT: Don't lead him. He's your witness.  
22 Ask him in a certain field what he has done in preparation  
23 for giving expert witness reports.

24 BY MR. CHARNES:

25 Q. Okay. Doctor Montgomery, in arriving at your opinions

1 relating to analyst reports, can you please describe to the  
2 Court what you did in the course of your review in arriving  
3 at your opinion.

4 A. I did several things. I reviewed the economic  
5 literature on analyst ratings, analyst reports and analyst  
6 forecasts, and their relationship to stock returns and other  
7 matters. I reviewed data on analyst reports. I analyzed  
8 the relationship, if any, between analyst ratings and stock  
9 returns using statistical and econometric techniques, and I  
10 reviewed a variety of other sources and information as well,  
11 such as news articles, SEC filings, in forming my opinions.  
12 Those are the main things that come to mind.

13 Q. In the course of arriving at your opinions related to  
14 the efficiency of the market related to the market  
15 hypothesis, could you please describe the activities you --

16 A. I relied on my general training as a financial  
17 economist. I reviewed economic literature on efficient  
18 market hypothesis and on deviations or anomalies from the  
19 efficient market hypothesis. I performed some of my own  
20 statistical analysis for this project also.

21 Q. In arriving at your opinions in this case as they  
22 relate to diversification, can you please explain what, if  
23 anything, you did by way of research and analysis.

24 A. Again, I relied on my training as a professional  
25 financial economist, and the study of diversification is an



1 integral part of that. I also performed numerical and  
2 statistical analysis of the degree of diversification in the  
3 plan, and the contribution of the two stock funds at issue;  
4 the NA Stock Fund and the NGH Stock Fund, and the level of  
5 risk, diversification being a means to reduce risk.

6 MR. CHARNES: That's all I have at this point,  
7 Your Honor.

8 MR. LEWIS: Just one, Your Honor.

9 BY MR. LEWIS:

10 Q. Can I direct you back to Plaintiff's Exhibit 239 --  
11 excuse me, 397, Doctor Montgomery, which, again, was your  
12 report.

13 A. Yes. I'm there.

14 Q. Did you just testify that you reviewed, in the course  
15 of arriving at your opinions on the efficient market, you  
16 reviewed the literature regarding anomalies with respect to  
17 the efficient market hypothesis? Did you testify to that,  
18 sir?

19 A. I'm generally familiar with that literature. I'm  
20 not -- I didn't rely on them in any way specifically to form  
21 these opinions.

22 Q. Did you just testify in answer to Mr. Charnes'  
23 question, that you had reviewed the literature on anomalies  
24 in the course of preparing your opinions in this case?

25 A. Yes. I believe that is true, yes.

1 Q. Let me direct your attention to Pages 4 and 5, on  
2 Exhibit 2 to your report, which is Plaintiff's Exhibit 397,  
3 and ask you to point out to me what article, if any, relates  
4 to the anomalies that have been found with regard to the  
5 efficient market hypothesis.

6 A. I believe the answer to the question related both --  
7 the question related both to -- maybe I misunderstood the  
8 question. But both my initial report and also to the  
9 follow-up report that I did that was reported in my  
10 supplemental report, I may not have looked at them in any  
11 detail for this initial report. Certainly based on this  
12 list, I didn't.

13 You know, if I can just add to that. In generally  
14 reviewing the financial economic literature as part of my  
15 professional work, I am familiar with the state of that  
16 literature and obviously, you know, bring that general  
17 familiarity to any work that I do. I don't obviously list  
18 the hundreds of articles that I review in the course of my  
19 work on these exhibits.

20 Q. Let me direct your attention to Defendant's Exhibit 64,  
21 which I guess --

22 THE COURT: Binder two.

23 THE WITNESS: I'm sorry, could you repeat the  
24 exhibit number?  
25

1 BY MR. LEWIS:

2 Q. Exhibit 64. And I direct your attention to the first  
3 page of that exhibit, which is titled Exhibit 1 on the top  
4 right-hand corner. I'm sorry, the first page of the report.  
5 The report has 31 pages, and then it is followed by Exhibit  
6 1. Is this a list of additional materials you reviewed in  
7 preparation of your supplemental report in this case?

8 A. Yes, it is.

9 Q. Is there anywhere on that list, where there is a piece  
10 of literature that listed -- that addresses any anomalies  
11 with regard to the efficient market --

12 A. None of these things I think specifically. Actually,  
13 I -- there is probably a discussion of anomalies in the  
14 Andrei Shleifer book.

15 THE COURT: Which one is that?

16 THE WITNESS: That's number 14, Inefficient  
17 Markets, An Introduction to Behavioral Finance, but I don't  
18 know that with certainty as I sit here.

19 BY MR. LEWIS:

20 Q. At your deposition did you testify that you were  
21 unfamiliar with the accrual anomaly?

22 A. I don't know what I testified. I'm not unfamiliar now.

23 Q. At the time you had your deposition taken, you had  
24 already prepared both of your reports; is that correct?

25 A. That's correct.

1 Q. Did you testify at your deposition, that you were  
2 unfamiliar with the accrual anomaly?

3 A. I don't remember.

4 Q. Let me point you to Page 4 of your deposition, please.  
5 I'm going to read the question again and ask you to read the  
6 answer, starting at Line 3, continuing through Line 18.

7 "Question: What is an accrual anomaly? Are you  
8 familiar with that term?"

9 A. "I'm familiar with the term. It is in, I believe, one  
10 of your expert's reports, and I believe it refers to a  
11 pattern of stock returns related to the -- the amount of  
12 accrued earnings and overall earnings reported by a  
13 company."

14 Q. "Are you familiar with any literature, other than what  
15 Mr. Lys may have referenced in his expert report with  
16 respect to accrual anomalies?"

17 A. "Nothing that I can specifically think of, no."

18 Q. "Is accrual anomaly as reported in the literature  
19 consistent or inconsistent with semistrong EMH?"

20 A. "I don't have an opinion about that."

21 Q. Is it also fair to say that at the time of your  
22 deposition, which was after you prepared your report in this  
23 case, that you had little familiarity with post-earnings  
24 announcement drift?

25 A. I don't know how you define "little." I understood the

1 issue, I believe, in general terms.

2 Q. Let me direct your attention to your deposition at Page  
3 190.

4 THE COURT: That was post-earnings what?

5 MR. LEWIS: Announcement drift.

6 BY MR. LEWIS:

7 Q. I'm going to ask you to start reading on Line 25 and  
8 all the way over to 192 and Line 18.

9 A. Are you going to read the question?

10 Q. Before we do that, let me ask one other question. Were  
11 you sitting in the courtroom during this trial when  
12 Professor Lys testified about post-earnings announcement  
13 drift?

14 A. Yes, I was.

15 Q. And were you sitting in the courtroom when Professor  
16 McEnally testified about post-earnings drift or earnings  
17 surprise as he claimed?

18 A. I was not here for Professor McEnally's testimony.

19 Q. Now we'll start reading at Page 190, Line 25.

20 "Question: What is post-earnings announcement drift?"

21 A. "Answer: My understanding of that is, that it's an  
22 empirical anomaly, and anomaly, if you will, that relates to  
23 a finding that a company's -- that stocks of companies that  
24 have positive earnings surprises tend to appreciate even  
25 after the earnings surprise is announced."

1 Q. "How long has that phenomena been the subject of the  
2 published information?"

3 A. "I'm not sure."

4 Q. "Is fair to say it goes back as far as the 1960's?"

5 A. "I don't know."

6 Q. "Have you read any articles or studies on that topic?"

7 A. "I've looked at some. I don't recall if I've read them  
8 in -- in -- completely."

9 Q. "So does this mean -- is the -- is the implication of  
10 post-earnings announcement drift that investors don't --  
11 strike that.

12 "Is the implication of post-earnings announcement drift  
13 that investors -- strike that -- that investors underreact  
14 to news about a company?"

15 A. "I think the -- the -- the empirical literature  
16 documents what it documents, which is just what I said.  
17 It's the tendency of stocks to continue to appreciate,  
18 whether that is a function of investors underreacting to the  
19 news or failing to appreciate the fact that additional  
20 positive news follows that additional positive earnings  
21 announcement. I think is -- I'm not sure. I believe that  
22 it's -- I believe it's still probably a subject of  
23 controversy" -- let me start again. "I believe that is  
24 still probably a subject of controversy, but I don't  
25 actually know."

1 Q. "Does the published literature establish post-earnings  
2 announcement drift exist for all stocks?"

3 A. "I don't know."

4 Q. "Including large -- does the published literature  
5 establish that although the drift may be less for large  
6 stocks than small, it still exists?"

7 A. "I don't know."

8 Q. "By large, I mean large cap. Did you understand the  
9 question?"

10 A. "Yes. But I still don't -- I still don't know the  
11 answer."

12 MR. LEWIS: Thank you.

13 I have no further questions, Your Honor.

14 THE COURT: Mr. Charnes, do you?

15 MR. CHARNES: Yes.

16 BY MR. CHARNES:

17 Q. Do you still have your deposition transcript, Doctor  
18 Montgomery?

19 A. Yes, I do.

20 Q. I would like to continue reading after where Mr. Lewis  
21 stopped on Page 192. Are you there?

22 A. Yes, I am.

23 Q. Again, I'll read the question, if you could read the  
24 answer, starting on Line 19.

25 "Is post-earnings announcement drift consistent or

1 inconsistent with semistrong efficient market hypothesis?"

2 A. "I think it depends on a debate as to the reasons for  
3 that, for the drift."

4 Q. "Well, it's not consistent for semistrong efficient  
5 market hypothesis, is it?"

6 There was an objection, and then --

7 A. My answer: "It depends on if this is a drift that  
8 investors could and did anticipate ahead of time."

9 Q. "Explain what you mean by that."

10 A. "The semistrong or any form of market efficiency  
11 involves whether there are predictable stock returns above  
12 the compensation for risk. What I believe this literature  
13 that you're referring to documents is the tendency of stock  
14 returns in past -- in a database of past returns. What I  
15 don't think it addresses specifically is whether investors,  
16 knowing that such" -- the transcript says attendance, I  
17 believe it is supposed to be such a tendency -- "that such a  
18 drift might occur failed to take advantage of it and buy the  
19 stock. And the question, I guess, comes down to whether  
20 it's reasonable to assert that investors know about this  
21 drift ahead of time and failed to act, and if that -- if you  
22 can assert -- if you can establish that, then you can  
23 establish that it's a departure from semistrong efficiency.  
24 I don't know enough about the literature on that particular  
25 issue to know if anybody has brought any evidence to bear on



1     that question."

2     Q.     Doctor Montgomery, you have reviewed the expert reports  
3     that Plaintiff has submitted in this case, have you not?

4     A.     Yes, I have.

5     Q.     And did you or did you not -- strike that.

6             Were you present in the courtroom for Professor Lys and  
7     Doctor Biller's testimony in this case?

8     A.     Yes, I was.

9     Q.     At any point either in their testimony or in their  
10    expert reports, had they suggested that the accrual anomaly  
11    has any application to the facts in this case?

12            MR. LEWIS:  Objection, Your Honor.

13            THE COURT:  I will allow him to answer that for  
14    the purpose of showing what he thinks he heard, not for the  
15    purpose of what actually the testimony was.

16            THE WITNESS:  Maybe you could repeat the question.

17    BY MR. CHARNES:

18    Q.     In either their expert reports or their testimony, have  
19    you -- any of the Plaintiff's experts argued that accrual  
20    anomaly applies in any way to the facts in this case?

21    A.     No, not that I'm aware of.

22    Q.     Have any of the Plaintiff's experts, in either their  
23    testimony here in court or reports, argued that  
24    post-earnings announcement drift has any application to the  
25    facts of this case?

1 A. No, they have not, to the best of my knowledge.

2 MR. CHARNES: Nothing further.

3 MR. LEWIS: Nothing further, Your Honor, other  
4 than argument.

5 THE COURT: And, Doctor Montgomery, perhaps you  
6 should step outside in the hall as we discuss this.

7 (The witness left the courtroom.)

8 MR. LEWIS: Your Honor, focusing on two specific  
9 areas that I questioned him about, let's take the last one  
10 first, which is efficient market hypothesis. Much of his  
11 opinions -- the heart of many of his opinions in the report  
12 rest on review that the semistrong efficient market  
13 hypothesis is a valid concept, extremely so in his case. I  
14 think he's testified that he's really done -- other than  
15 what he got generally when he went to school, he really  
16 doesn't have any particular expertise in the efficient  
17 market hypotheses. He hasn't published on it, he hasn't  
18 written on it, he hasn't taught on it.

19 Both Professor McEnally and Professor Lys  
20 testified it was one thing they did agree about, that two of  
21 the major departures on the efficient market hypotheses in  
22 the literature were accrual anomaly and post-earnings  
23 announcement drift.

24 The witness, at the time of his deposition, that  
25 late, really had never heard of the accrual anomaly, and had

1 little familiarity. I think Mr. Charnes, the excerpt  
2 Mr. Charnes had him read, at the end of it, as well as the  
3 excerpt I read, little familiarity with the post-earnings  
4 announcement drift, which is the major one document in the  
5 literature.

6 He testified that he -- if you look at the  
7 exhibits to his reports, he evidently did not review any of  
8 the literature on any of these anomalies in the course of  
9 preparing his report.

10 The issue isn't whether Professor Lys or Doctor  
11 Biller said that that, either of those concepts has specific  
12 analysis, specific applicability to the facts of this case,  
13 the issue is, Doctor Montgomery rests his opinions on the  
14 efficiency of the markets, the semistrong form of market  
15 efficiency and, therefore, for him to be unfamiliar with the  
16 two major deviations to it documented in the academic  
17 literature, shows he's not truly an expert on that.

18 I don't see how somebody could be expert on it, if  
19 they haven't read the major literature with regard to its  
20 failings. That's on efficient markets.

21 THE COURT: I'm going to allow him to testify on  
22 that, subject to your cross-examination, which you may  
23 choose to stand on what you have already asked, or you may  
24 ask further questions, as that goes to the weight of the  
25 value of his opinion.

1           MR. LEWIS: Again, I think with regard to the  
2 other subjects as well that I questioned him about;  
3 diversification primarily, what individual experienced  
4 investors do in terms of securities and securities  
5 selection, I don't think -- again, he has general knowledge  
6 of finance and economics, I don't dispute he's an expert in  
7 that, kind of macro economic issues, but I don't think he's  
8 shown expertise in the particular areas of diversification;  
9 securities analysis, buying and selling of individual  
10 securities or diversification -- or I'll leave it at those  
11 two. Again, I assume Your Honor's ruling would be similar  
12 on those.

13           THE COURT: Yes. I think he has sufficient  
14 training and experience to state an opinion in that field.  
15 The extent to which that opinion should be valued, I think  
16 is subject to examination you've already made and any  
17 further examination that you undertake.

18           MR. LEWIS: Thank you, Your Honor. Would this be  
19 a good time to take a midmorning recess?

20           MR. CHARNES: I think so, Your Honor.

21           THE COURT: Let's do that.

22           Doctor Montgomery, we're going to take a  
23 midmorning recess, so you may come down off the stand and  
24 we'll be back in about 15 or 20 minutes.

25           (Recess taken from 11:20 a.m. to 11:45 a.m.)

1 BY MR. CHARNES:

2 Q. Welcome back, Doctor Montgomery.

3 A. Thank you.

4 Q. Will you please turn to Defendant's Exhibit 60. Do you  
5 have that in front of you?

6 A. I do. Okay.

7 Q. What is Defendant's Exhibit 60?

8 A. This is a copy of my initial expert report for this  
9 case, dated April 18, 2008.

10 Q. And if you please turn to Exhibit 61 and identify that  
11 for the record, DX 61.

12 A. Sixty-one? Exhibit 61 is a list of corrections,  
13 primary typographical or numerical to the initial expert  
14 report.

15 Q. And read together, do Defendant's Exhibits 60 and 61  
16 accurately contain expert opinions you have formed in this  
17 case?

18 A. Yes, they do.

19 Q. With respect to the damages opinions in Defendant's  
20 Exhibits 60 and 61, have they been subsequently updated  
21 after you wrote those documents?

22 A. Yes, they have. They've been updated in two ways. I  
23 can provide detail on them when you want. For recent, more  
24 recent financial returns and also for an updated list of  
25 release signers.

1 Q. If you now turn to Defendant's Exhibit 64. If you  
2 could identify that for the record.

3 A. This is a copy of my supplemental report in this  
4 matter, dated July 15th, 2008.

5 Q. And if you could please identify Defendant's Exhibit  
6 65.

7 A. Defendant's Exhibit 65 is a list of corrections to the  
8 supplemental report.

9 Q. And what sort of corrections did DX 65 make to DX 64?

10 A. They are primarily typographical or minor numerical  
11 changes.

12 Q. And again with the exception of the damages numbers,  
13 which I understand you testified have been updated, do  
14 Defendant's Exhibits 64 and 65, read together, accurately  
15 contain the expert opinions you formed in this case?

16 A. Yes, they do.

17 Q. If you would please turn to DX 67. Are you there,  
18 Doctor Montgomery?

19 A. I am there.

20 Q. What is Defendant's Exhibit 67?

21 A. This is a supplement -- I guess it's actually an update  
22 to certain exhibits in the expert report and supplemental  
23 expert report. The update, as it says in the first  
24 paragraph, the updates reflect information about additional  
25 plan participants who have signed releases, and they also

1 reflect data on recent returns on Plan investments and on  
2 market financial returns.

3 Q. You may have just said this, but what is the date of  
4 these updates?

5 A. I think I forgot to say. It's June 5th, 2009.

6 Q. And after this -- after Defendant's Exhibit 67, did you  
7 further update your exhibits to your reports related to  
8 damages?

9 A. Yes, I have. The most recent updates reflect financial  
10 returns and Plan returns through September 30th, 2009 that  
11 is the end of the third quarter of 2009, and also release  
12 signers up until November 30th, 2009.

13 Q. And if you would please review Defendant's Exhibits 244  
14 through 251 and then 282, and we can go back with those  
15 numbers, and confirm that those exhibits reflect your  
16 updated damages information.

17 A. I'm going to need to turn to a different binder.

18 MR. CHARNES: It should be in binder four, Your  
19 Honor.

20 THE WITNESS: Okay. Sorry. I believe you said  
21 starting with Defendant's Exhibit 244?

22 BY MR. CHARNES:

23 Q. 244 to 251, and then 282.

24 A. Okay. 244, 245, 246, 247, 248, 249, 250 and 259 are  
25 all --I'm sorry, I misspoke. 250 and 251, are all exhibits

1 providing the updated -- the most updated estimate of  
2 damages in various scenarios for this case.

3 Just remind me of the last exhibit, please.

4 Q. 282. DX 282.

5 A. Yes. This is the update of the returns that are --  
6 feed into the damages calculations that were in the other  
7 exhibits.

8 Q. 282 is an update of those?

9 A. Of the financial returns, yes.

10 Q. Doctor Montgomery, if you please turn to Defendant's  
11 Exhibit 239. It should be in that same binder. Do you have  
12 239, Doctor Montgomery?

13 A. I have it. Does the Court have it?

14 THE COURT: I think I do.

15 THE WITNESS: Okay. Good.

16 BY MR. CHARNES:

17 Q. What is Defendant's Exhibit 239?

18 A. 239 is a summary of my three main opinions related to  
19 liability matters in this case.

20 Q. Who created these summaries?

21 A. I created the summaries. The lawyers helped me, the  
22 law firm helped me prepare the actual exhibit.

23 Q. The words on Exhibit 239 are your's?

24 A. Yes, they are.

25 Q. Would using Defendant's 239 today assist your



1 testimony?

2 A. Yes, it would.

3 Q. If you would please turn to your first opinion listed  
4 on DX 239, would you please explain to the Court what your  
5 opinion is.

6 MR. LEWIS: Your Honor, can we have a standing  
7 objection on this one, pursuant to the colloquy we had  
8 earlier this morning?

9 THE COURT: Of course.

10 BY MR. CHARNES:

11 Q. What is your first opinion, Doctor Montgomery?

12 A. My first opinion is, there was no reason in 1999 or  
13 2000 to expect returns from NGH or NA that were in excess of  
14 what could be achieved from two alternative ways to put the  
15 same concept. One is the way it's written in this exhibit  
16 now, to -- in excess of what could be achieved from  
17 diversified investment funds.

18 The other way to put that, which is the way I expressed  
19 it in my report, there is no reason to expect extraordinary  
20 returns, and by extraordinary -- and sometimes you hear this  
21 called abnormal returns, Professor Lys used in his  
22 testimony, and those are returns beyond the return that the  
23 market will provide based on -- basically the returns beyond  
24 what the market provides to a diversified investment,  
25 basically beyond the returns in the market, adjusted for

1 whatever the overall market risk is of a particular  
2 investment, in this case, NGH or NA.

3 Q. And what is the basis of that opinion?

4 A. I think there are three primary bases for this opinion.  
5 The first is, I think, essentially, basically for want of a  
6 better word, a common sense approach, and that is, the  
7 market consists of thousands, if not millions of investors  
8 each seeking to find some informational edge to exploit --  
9 to get the highest possible return they can for the lowest  
10 amount of risk, and if there were public information out  
11 there in the market that would have led people to expect  
12 that either of these stocks would have a better return, a  
13 greater return than the market as a whole or other stocks  
14 which are represented by the market average, participants  
15 who didn't -- I'm sorry, investors who didn't own either of  
16 these stocks would be rushing to buy them. That process  
17 would be bidding up the price.

18 Conversely, investors who already held them, would  
19 be -- and may have had plans for whatever reason to sell  
20 them, would have said, well, wait I minute, I expect  
21 extraordinary returns, I'm not going to sell these stocks  
22 now.

23 Both of those things together would create a demand  
24 for the stocks and they would, quite quickly, and in a  
25 matter of hours, if not quicker, would bid up the price of

1 those stocks, and whatever that public information would  
2 quickly be reflected in the stock price, such that there  
3 would no longer be any predictable extraordinary returns to  
4 be had by investing in the stock, and I think that's --  
5 essentially it is common sense, when you think about how the  
6 market works and what all the investors in the market are  
7 doing as well as all the media covering the market.

8 The second opinion relates to something called the  
9 efficient market hypothesis.

10 Q. You mean the second basis?

11 A. Excuse me, the second basis, yes. The second basis for  
12 my first opinion is essentially, the efficient market  
13 hypothesis.

14 Now, the efficient market hypothesis, which is a  
15 theoretical statement that they are essentially the same  
16 thing, there are no -- there is no ability to achieve  
17 returns, extraordinary returns for any particular financial  
18 investment greater than one could achieve from any other  
19 investment. Basically there are no extraordinary returns  
20 available in the market. There are three versions of that.  
21 There is the weak form, which has to do with no reason to  
22 expect extraordinary returns based on the past performance  
23 of the stocks, their stock prices or returns. The  
24 semistrong, which says that there is no ability to achieve  
25 extraordinary returns based on public -- any publicly

1 available information, and those are the two that are really  
2 relevant to my opinion here. There is also something called  
3 strong form, which says there is no -- when there is no  
4 ability to achieve extraordinary returns, even relying on  
5 insider information, and that's probably not in anybody's  
6 estimation correct.

7 The efficient market hypothesis, if it is true for NGH  
8 or NA, would also imply that there are no extraordinary  
9 returns to be had based on public information. The  
10 efficient market hypothesis, I should say is basically an  
11 academic, "formulation" of the common sense view that I  
12 already gave you as my first basis.

13 I performed a series of tests of the efficiency of the  
14 markets for NGH and NA. These tests are all tests that have  
15 been considered by courts in securities class action  
16 litigation, where the establishment of the efficiency of the  
17 market is an important part of the establishment that  
18 investors could rely on whatever public information is at  
19 issue in those cases.

20 I have an exhibit in my expert report that goes through  
21 the tests, the details of these tests; several exhibits,  
22 rather, for NGH and NA, and in almost all cases, the results  
23 strongly support the conclusion that the market for both NGH  
24 and NA was efficient during 1999 and early 2000.

25 Q. If you would please turn to Defendant's Exhibit 240.

1 What is Defendant's Exhibit 240?

2 A. This is a summary of the tests that I ran on the  
3 efficiency of the markets for NGH and NA.

4 Q. I was just going to ask if Defendant's Exhibit 240 is a  
5 summary of the information provided in six and seven in your  
6 initial expert report, DX 60.

7 A. Just have to make sure that I have the exhibit numbers  
8 right.

9 Q. Take your time.

10 A. Yes, it is.

11 Q. Does Defendant's Exhibit 240 accurately represent the  
12 findings in your expert report?

13 A. Yes, it does.

14 Q. Would using DX 240 assist your testimony today?

15 A. Yes, it would.

16 Q. Would you, please, using Defendant's Exhibit 240 as you  
17 need to, if you would please describe for the Court what  
18 your findings were with respect to market efficiency.

19 A. Okay. It would probably be helpful as I do this to  
20 also -- I'm going to refer to some of my exhibits in my  
21 expert report, just because they provide more detail, but  
22 the summary is again on Exhibit 240.

23 The Exhibit 240 reports the results of six tests. The  
24 first four of these tests, were tests that were outlined in  
25 the Cammer decision, that is, I believe -- my understanding

1 was the original decision that dealt with the test for  
2 efficient markets. The last two were other tests that have  
3 been in other decisions. The first test looks at the  
4 average weekly trading volume for the stocks, and the idea  
5 behind this is that the more stock that is being traded on a  
6 weekly basis over any period of time, the more investors are  
7 active in the market, making buying and selling decisions,  
8 so any information that's available in the public domain,  
9 those buyers and sellers will be looking at that information  
10 in making their decisions about buying or selling the stock  
11 and, therefore, the prices will more accurately and more  
12 quickly, I shouldn't say accurately, but they would more  
13 quickly reflect any public information.

14 The average weekly trading volume for NGH was about  
15 2.1 percent of the shares outstanding, and the average  
16 weekly trading volume for NA, was 3.24 percent, and both of  
17 these are above the 2 percent level cited by the Cammer  
18 criteria as providing evidence in favor of an efficient  
19 market, and they do both to me, appear to indicate that  
20 there was a substantial amount of trading volume in the  
21 stocks.

22 The second test also in Cammer is, the number of  
23 securities analysts covering the stock, and in order to do  
24 this, I derived from the IBES database analysts who were  
25 providing earnings statements and earnings forecasts for the

1 stock. I found that there were 11 analysts covering NGH and  
2 19 analysts covering NA. These are all sell-side analysts  
3 working for brokerage firms and banks that have been  
4 discussed in other testimony.

5 Both of those -- in both cases, there is a substantial  
6 amount of analysts, and I believe supports the conclusion of  
7 the efficiency for both of these stocks.

8 There are many people who are -- as part of their  
9 professional activities -- are acquiring, interpreting and  
10 processing public information, and this is part of the  
11 process by which the public information gets reflected in  
12 the stock prices.

13 The third condition, also a Cammer decision is, the  
14 eligibility of the companies to file an S3 registration  
15 statement with the SEC, and that's a more abbreviated  
16 registration statement that is permitted for more  
17 established companies. Both companies were eligible to file  
18 such statement, and that, in my mind with the Cammer  
19 decision, also supports efficiency.

20 The fourth test is the price response to unexpected  
21 news, and this, I think, is the most directly relevant test  
22 to efficient market, because it looks directly at whether  
23 publicly -- new public information, that is new news, gets  
24 reflected in the stock price, whether new news tends to move  
25 the stock price to a different level either up or down,

1    whereas -- and if it moves the stock, the stock moves more  
2    on days where there is news being released, then it does on  
3    other days. In order to do this -- and the details of this  
4    is reported in separate tables in my expert report.

5           In Exhibits 9 and 10 of Defendant's Exhibit 60, I  
6    identified three fairly standard sources of news that might  
7    be relevant to investors. They are earnings announcements,  
8    dividend announcements, and acquisition announcements. I  
9    tested to see whether the abnormal returns of NGH and NA on  
10   days when there was this sort of announcement had a tendency  
11   to be larger than the abnormal returns were on days when  
12   there wasn't any information, and I indeed found that there  
13   were more days proportionately that were with large returns  
14   when there was also news being released, then there were on  
15   days when there wasn't being released. So that suggests  
16   that news has a tendency to move the stock, and move it more  
17   than just regular buying and selling. This, in turn,  
18   supports the conclusion that the stocks both had a fast  
19   response to unexpected news and in terms supports the idea  
20   of the fact -- supports the conclusion that both of these  
21   stocks traded in an efficient market.

22           Those four I've just discussed are the four conditions  
23   that are mentioned in the Cammer decision, and my  
24   understanding is, they've also been mentioned in a number of  
25   other decisions.



1       There are two other conditions that have been mentioned  
2 in other cases that we've also looked at for this case. One  
3 is the overall market capitalization of the stock, and  
4 actually, I should probably stop and define what market  
5 capitalization is, because the idea comes up in a few areas  
6 in my testimony and in my opinions.

7       Market capitalization is the total value of the shares  
8 of stock outstanding of a particular company. If you look  
9 at all of the shares, let's say that NGH distributed at the  
10 time it may be a hundred million dollars, and that stock was  
11 worth, say, \$20 a share, then the market capitalization  
12 would be a hundred million times \$20 a share, or  
13 \$2 million -- \$2 billion, rather. So that's market  
14 capitalization, overall values of shares in the market.

15       Both of these stocks were basically large cap stocks.  
16 NGH's market capitalization range from 2.7 billion to  
17 5 billion during the period from June 15, '99 through  
18 January 31st, 2000. That is the large market capitalization  
19 that favors a conclusion of efficiency.

20       NA's market capitalization, if you only look at  
21 20 percent of the stock that was traded in the market, was  
22 1.5 to 2.3 billion, that's also a substantial market  
23 capitalization and favors market efficiency.

24       The final test that I ran, and the only one where the  
25 results are mixed is, the size of the bid ask spread. The

1 size of the bid ask spread is the difference between the  
2 highest quote to buy the stock among the market makers and  
3 the lowest stock quote to sell the stock among market  
4 makers, and this spread was somewhat -- for NA and NGH, was  
5 somewhat wider than the average or typical stock.

6 Having said that, both of these stocks traded on the  
7 New York Stock Exchange, which is a very well-established  
8 and generally efficient stock market, and I understand there  
9 are actually some courts that have generally recognized the  
10 New York Stock Exchange as being an efficient stock market.

11 So any way, that's a summary of the tests I ran of  
12 market efficiency, and they support my conclusion that both  
13 NGH and NA generally traded in efficient stock range.

14 Q. Doctor Montgomery, based on your experience, are the  
15 tests you just performed the ones that are used by  
16 economists to analyze market efficiency and fraud on the  
17 market, based on the fraud on market theory in security  
18 fraud cases?

19 A. Yes. Well -- sorry, your question is, is it my  
20 experience that these are the tests --

21 Q. I apologize for the poor question. Based on your  
22 experience, the tests that you -- that you just testified  
23 to, are those tests economists perform in order to determine  
24 market efficiency for fraud on the market in securities  
25 fraud cases?

1 A. Yes, they are.

2 Q. You said there are three bases for your opinion. What  
3 is the third basis for your opinion?

4 A. The third basis is a set of three statistical or  
5 econometric -- econometric is really the application of  
6 statistics to economic data. There are three econometric  
7 tests of behavior of NA and NGH Stock prices and they also  
8 support efficiency.

9 Q. Are those three tests described in detail in your  
10 expert report?

11 A. Yes, they are. All three tests support efficiency.

12 Q. Could you point out where they are located in your  
13 expert report, DX 60?

14 A. Yes. In DX 60 the results of the tests, I believe they  
15 are discussed in the text of the report, of course, but the  
16 exhibits summarizing the test is Exhibit Number 10.

17 Q. Thank you.

18 THE COURT: And the best way to get to Exhibit  
19 Number 10?

20 THE WITNESS: Depends on where you are.

21 THE COURT: I got Exhibit 10, page one of one.

22 THE WITNESS: Yes. It's only one page.

23 BY MR. CHARNES:

24 Q. Could you briefly summarize what those three tests are  
25 in the results?

1 A. Yes. The first test is a test for something called  
2 serial correlation. Serial correlation is a test, and the  
3 footnotes of this exhibit provides a lot of detail, but  
4 serial correlation is a test that examines the extent to  
5 which a stock's return on a particular day are useful in  
6 predicting its return on the next day.

7 A positive serial correlation would imply that a  
8 positive abnormal or excess return would be followed by  
9 another positive abnormal or excess return.

10 Negative serial correlation would mean that a positive  
11 return would be followed by a negative return, and if that  
12 were true, it would suggest that the market is not efficient  
13 in the weak form sense, and that past stock return is useful  
14 for predicting a future stock return.

15 The tests for serial correlation for both NA and NGH,  
16 basically fail to reject the hypothesis that there is no  
17 serial correlation, and so the test supports the conclusion  
18 that both NA and NGH were efficient with regard to this  
19 test.

20 The second test is a test of the tendency of a stock to  
21 overreact to news, and this is based on a selection of days  
22 in which either NA or NGH had a large return, that is a  
23 return that is statistically significant, the 5 percent  
24 level which is a standard measure of statistical  
25 significance, and it's a test of whether days with a

1 large -- that is statistically significant return, tend to  
2 be followed in any of the next ten days by either additional  
3 returns, additional positive returns, additional returns  
4 either in the same direction or in the opposite direction,  
5 so basically, our large returns generally followed by other  
6 large returns, more than you would expect just by looking at  
7 random, a random selection of days. When you do this test,  
8 the results also support null hypothesis that the markets  
9 are efficient, there is no tendency of stocks to overreact  
10 or underreact to news.

11 Finally the third test is based on a paper by authors,  
12 by the name of Lo and MacKinlay. Lo and MacKinlay test the  
13 variability or variance of stock returns over time. If the  
14 markets follow a form -- follow something called a random  
15 walk, which is that every stock return is basically  
16 unpredictable and either could either be randomly up or  
17 randomly down on any day, and that's kind of a narrow --  
18 somewhat restricted version of efficient market where there  
19 is no ability to predict anything about stock returns from  
20 day-to-day. An implication of a random walk is, that the  
21 variability of a stock's return is exactly proportional to  
22 the length of time that the return is calculated over, so  
23 that a two day return would have twice the variability of a  
24 one day return. A three day return would have three times  
25 the variability of a one day return, and so forth. And

1 that's the basic idea behind the Lo and MacKinlay test and  
2 running this test on NGH and NA also supports a finding of  
3 efficiency for NGH and NA. That's a summary of the three  
4 tests that I did.

5 Q. And in your opinion, Doctor Montgomery, what are the  
6 implications of your findings with respect to whether the  
7 above market or abnormal returns could have been anticipated  
8 into the year 2000 for NGH and NA?

9 A. Well, all of these -- all of this analysis supports,  
10 again, the conclusion that the markets for NA and NGH were  
11 generally efficient, at least in 1999 and 2000, and in an  
12 efficient market, there is no ability for investors to  
13 predictably make extraordinary returns based on publicly  
14 available information.

15 Q. Will you please turn back to Defendant's Exhibit 239,  
16 which is the summary of your opinions.

17 A. Okay.

18 Q. What is your second major opinion, Doctor?

19 A. My second major opinion is, that the removal of the NGH  
20 and NA from the Capital Investment Plan, did not raise, and  
21 in fact lowered the risk level borne by the vast majority of  
22 plan participants.

23 Q. And what is the basis for that opinion?

24 A. The basis for that opinion is, an analysis that I  
25 carried out of the levels of risk of NGH and NA in the Plan,

1 their correlation with other investments, and specific  
2 analysis of the levels of risk borne by each participant in  
3 the CIP in 1999 and 2000, and the effects of eliminating NGH  
4 and NA on the risk levels for each of those participants.

5 Q. Before we turn to the specific analysis that you did,  
6 as with your first opinion, do you have a common sense  
7 explanation of this opinion for the Court?

8 A. Well, I think the common sense opinion is, that single  
9 stock funds like NA or NGH, are riskier than diversified  
10 stock funds, like the total stock market fund, which was one  
11 of the options in the Plan, and the reason is, that a  
12 diversified investment funds aggregates investments in  
13 numerous different stocks, and the particular risks of  
14 investing in each of those stocks, tends to cancel each  
15 other out, and that's the basic process of diversification,  
16 if you only hold a little bit of this stock, a little bit of  
17 that stock, et cetera, they won't all go up at the same time  
18 and down at the same time, so your overall risk is  
19 substantially less, and that's the basic principle of  
20 diversification.

21 Q. Did you just testify that in addition to that basic  
22 principle of diversification, you also undertook analysis to  
23 determine a level of risk in this Plan?

24 A. Yes, I did.

25 Q. Would you please turn to Defendant's Exhibit 241. What

1 is Defendant's Exhibit 241?

2 A. This is a summary of the analysis of plan risk that I  
3 performed.

4 Q. And is the information on Defendant's Exhibit 241,  
5 summarized in your analysis in Exhibits 19 and 22 of your  
6 report, DX 60?

7 A. Yes. It does summarize the analysis presented in those  
8 exhibits and in the text of those reports.

9 Q. Would DX 241 assist your testimony today?

10 A. Yes, it would.

11 Q. With reference to DX 241, would you please explain the  
12 work that you performed to help you reach your second  
13 opinion.

14 A. Yes. There really are four different stages of the  
15 work. The first involves the calculation of volatility.  
16 Now, volatility is the variability of a particular  
17 investment stock or mutual fund or portfolio of multiple  
18 investments. I analyzed this by calculating the historical  
19 variability of daily returns of each of the investment  
20 options within the CIP, including the NGH and NA Common  
21 Stock Funds. My findings for NGH and NA are in the two  
22 columns at the right of the Exhibit 241.

23 For NGH, I found that it had the -- NGH had the second  
24 highest volatility among Plan options. The highest  
25 volatility by the way was the RJR Tobacco Common Stock Fund.



1 I also found that NA had the third highest volatility  
2 among the Plan options and, subsequently, all the  
3 diversified investment funds within the Plan had lower  
4 volatility than these single stock funds.

5 The second piece of analysis that I performed involved  
6 an analysis of the correlation of the returns of NA and NGH  
7 with other options within the Plan. The importance of  
8 correlation is a basic statistical concept, and it's the  
9 tendency of two investments to have high returns at the same  
10 time, or conversely low returns at the same time. The  
11 higher the correlation of the two investments have with each  
12 other, the less benefit you get from diversification from  
13 investing in those two investments together. When you  
14 diversify you want to try to choose investments that have  
15 low correlation with each other.

16 So, I calculated the correlation of NGH and NA's Common  
17 Stock Fund returns with each of the other investments in the  
18 Plan. I found that NGH's returns were highly correlated,  
19 very highly correlated with the returns on RJ Reynolds  
20 Tobacco Common Stock. That's not surprising, because both  
21 of these stocks had exposure to tobacco litigation, and it's  
22 not surprising that their daily returns would be highly  
23 correlated, reflecting changes in the perception of the risk  
24 of tobacco litigation.

25 I found that NA had lower correlation with RJ Reynolds

1 Tobacco Stock, but it is also -- I found that NA was held by  
2 far fewer participants than NGH. NGH was held by many  
3 participants because those participants had been investing  
4 in their company stock, that is RJR Nabisco, before the  
5 spin-off, and then after the spin-off, they simply retained  
6 the positions that resulted from the spin-off, without  
7 taking any addition to adjust those -- any action to adjust  
8 those positions, either positively or negatively.

9 NA had to be a more active decision by participants,  
10 and I found relatively few participants that undertook that  
11 active decision to hold NA Stock.

12 The third piece of the analysis I did was, I used data  
13 on Plan transactions and Plan balances and Plan values that  
14 I was provided in this case, to calculate the impact for  
15 each Plan participant's total account in the CIP to  
16 calculate the impact of removing hypothetically the  
17 investments in NGH and NA from their Plan accounts on  
18 June 14, 1999, and what the impact would be on their total  
19 level of volatility, that is risk in their Plan accounts,  
20 basically compared to the level of risk, including NGH and  
21 NA, whatever positions they actually had with the level of  
22 risk of hypothetically taking those NGH and NA investments  
23 out on June 15th. My conclusion was, that the level of  
24 risk decreased for the vast majority of participants. About  
25 80 percent of the participants saw a risk of some degree in

1 the level of risk of NGH and NA were removed.

2 The final piece of the analysis I did was somewhat  
3 similar to the previous one, but instead of looking at what  
4 would have happened if hypothetically NGH and NA had been  
5 removed on June 15th, I looked at what actually happened  
6 after NGH and NA were ultimately removed from the Plan on  
7 June 31st, 2000, and I analyzed the portfolios of every Plan  
8 participant who held either NGH or NA or both, on  
9 January 31st, 2000, and these would be the participants  
10 whose investments in those stocks would have been  
11 transferred into the interest income investments on  
12 February 1st. In order to give them some time to make any  
13 adjustments they might have wanted to make in their  
14 investments after that transfer to interest income, I looked  
15 at their investment portfolios as of the end of February,  
16 one month later, February 29th, 2000, and I calculated the  
17 level of volatility of each participant's portfolio. I  
18 compared that level of volatility of risk with the level of  
19 volatility of risk right before NGH or NA were removed on  
20 January 31st, 2000, and I found, similar to my analysis for  
21 June 15th, I found that removing -- the actual removal of  
22 NGH and NA resulted in reduction of risk for the vast  
23 majority of participants, in this case, about 75 percent of  
24 participants saw a reduction of their level of risk.

25 Those are -- that's a summary of the four different

1 ways that I analyzed the impact of NGH and NA on the risk  
2 borne by Plan participants.

3 Q. To your knowledge, Doctor Montgomery, did any of  
4 Plaintiff's experts perform a comparable risk analysis  
5 related to the Nabisco Funds?

6 A. No. To my knowledge, they did not. I believe  
7 Plaintiff's experts made some statements about the effect  
8 that if NGH and NA had been optimal from a risk standpoint  
9 before June 14th, they would be at least as optimal after  
10 June 14th, and that was based on, I think, as far as I know,  
11 unsubstantiated views about the correlation of NA and NGH  
12 with other investments, but there was no effort to actually  
13 analyze the risk that I'm aware of by either of Plaintiff's  
14 experts.

15 Q. Doctor Montgomery, one may argue that the participants  
16 who held NGH or NA Stock in their Plan accounts made the  
17 choice to do so and, therefore, voluntarily assumed the  
18 greater risk to which you've just testified. Do you have an  
19 opinion as to whether such an argument would be correct or  
20 not?

21 MR. LEWIS: Your Honor, objection.

22 THE COURT: Doctor Montgomery, do you mind  
23 stepping out in the hall.

24 THE WITNESS: Not at all.

25 *(The witness left the courtroom.)*

1           MR. LEWIS: I don't think there is any -- he's not  
2 qualified as an expert in the psychology of 401(K) plan  
3 participants, as to why they make decisions they do, as to  
4 what they do. He said he has no experience consulting with  
5 or helping administer 401(K) plans, unlike Mr. Altman, for  
6 example, so I think it's outside his area of expertise, Your  
7 Honor. We're heading to an opinion as to what participants  
8 do or don't choose to do.

9           MR. CHARNES: Your Honor, I can try to rephrase.  
10 He actually analyzed the participant data and reached  
11 opinions on that data, as to behavior of the participants in  
12 the Plan. He's not testifying, as he made clear, I think on  
13 voir dire, that he's not testifying about the investment,  
14 he's not qualified to talk about the investment behavior of  
15 any particular person, but based on his training and  
16 experience and on his analysis of a million plus pieces of  
17 data here, he will be testifying about his actual -- the  
18 results of his study about the participant data and what  
19 they show.

20           As I said, I think I can try and rephrase the  
21 question, if Your Honor has a concern with the way it was --

22           THE COURT: I do have a concern about the way it  
23 was phrased. I don't know -- how do you intend to rephrase  
24 it?

25           MR. CHARNES: Well, I think I can ask him if he's

1 studied the behavior of participants -- strike that.

2 I can ask him if he's studied the actions taken by  
3 participants in the Plan, based on the data he has, which is  
4 over the period of 1997 to, I believe, 2002. And if he has  
5 a conclusion as to whether participants -- as to what  
6 proportion of participants were making active -- based on  
7 the data that he analyzed, whether participants were  
8 actively managing their accounts or not.

9 THE COURT: Do you object to that?

10 MR. LEWIS: It depends on the ultimate form of the  
11 question as the conclusion, Your Honor. I don't have any  
12 objection -- I don't know that he's particularly qualified  
13 to do this statistical study, not having experience  
14 administering 401(K) plans, familiarity of the records, but  
15 if he just gives the numbers, that's fine, but I think I may  
16 still have an objection when we get to the punch line, when  
17 Mr. Charnes gets to the punch line.

18 THE COURT: Why don't we go there and see where we  
19 are.

20 BY MR. CHARNES:

21 Q. Doctor Montgomery, do you have in your possession data  
22 regarding participant -- strike that.

23 Did you have in your possession data regarding the  
24 activities of participants in their accounts?

25 A. Yes, I do.

1 Q. And what was the period of time for which you had that  
2 data?

3 A. It was from the middle of 1997 through the end of 2002.

4 Q. And did you do any work to analyze that data to  
5 determine the activity of participant changes -- strike  
6 that.

7 Did you do any work using that data to determine how  
8 frequently participants in the Capital Investment Plan made  
9 changes to their Plan account?

10 A. Yes, I did.

11 Q. What was the conclusions of that study?

12 A. The analysis that I had staff under my direction  
13 perform looked at transfers, voluntary transfers that  
14 participants made from one investment fund to another, and  
15 these would be transfers that participants might undertake  
16 if they wanted to reallocate their investments based on  
17 changing -- their changing perceptions of risk or their  
18 changing views of investments, whatever. And I think they  
19 would be indicative of Plaintiff's -- I'm sorry,  
20 participants taking an active role in managing their  
21 portfolio.

22 At any rate, we looked at the number of participants  
23 who had no voluntary transfers over the entire data set that  
24 is from mid 1997 through the end of 2002, which I think is  
25 five and a half years, if I'm calculating it correctly, and

1 I found that there were about 1,500 of the approximately  
2 3,500 participants in the data set had no voluntary  
3 transfers whatsoever. I believe the exact number was 1,568,  
4 but I may have that off a little bit.

5 THE COURT: Are these total participants in the  
6 CIP?

7 THE WITNESS: No, Your Honor. They are the -- it  
8 is the data set that we were informed were all the  
9 participants who had a position in either NA or NGH on June  
10 15th, 1999. So they are all the participants who are  
11 potentially members of the class.

12 BY MR. CHARNES:

13 Q. So approximately 45 percent?

14 MR. LEWIS: Excuse me, move to strike everything  
15 in the answer up to the point where he said, "We looked at  
16 the number of people." All of the beginning of it was  
17 speculation and opinion on what people might or might not  
18 have been thinking, in terms of risk, et cetera.

19 THE COURT: Okay. I will not consider that up to  
20 this point.

21 MR. LEWIS: Thank you.

22 BY MR. CHARNES:

23 Q. Doctor Montgomery, is your testimony that approximately  
24 45 percent of the participants who held NGH and or NA as of  
25 the time of the spin-off, never made a voluntary transfer



1 during the time period you examined?

2 A. If the math is right, about 1,500 is about 45 percent  
3 of 3,500, sounds about right.

4 THE COURT: You do the math before you agree.

5 MR. CHARNES: Your Honor, I'll withdraw the  
6 question.

7 BY MR. CHARNES:

8 Q. Doctor Montgomery, did you also compare the holdings of  
9 participants who were -- whose NGH and NA shares were sold  
10 on January 31st, with their holdings as of June 14th, 1999?

11 A. Yes, I did.

12 Q. What were the conclusions of that analysis?

13 A. Well, the comparison is slightly broader than your  
14 question stated. It was a comparison -- it was an  
15 examination of their holdings of both NGH, which was the --  
16 had been the former RJR Nabisco Stock, and also their  
17 holdings of RJR Tobacco Stock, which was the stock they  
18 would have received as a result of the spin-off, so  
19 everybody who held RJR Nabisco Stock on June 14th, received  
20 NGH and RJR Tobacco Stock, and I found that for many --  
21 forgetting if it was most, but many, fairly certain it was  
22 most participants who had positions in NGH as of January  
23 31st, 2000, most of them had not done anything to change  
24 either their RJR Tobacco or their NGH positions since the  
25 spin-off, that is, they held exactly the same positions on

1 January 31st, that they had held on June 15th.

2 THE COURT: And I'm not sure how helpful that is.  
3 Any, most. I'm not sure how to process that information,  
4 Mr. Charnes.

5 BY MR. CHARNES:

6 Q. Doctor Montgomery, would it help you to refer to your  
7 expert report to put a little bit more meat on the bones, so  
8 to speak?

9 A. Yes, it would.

10 Q. If you refer, please, to DX 64, which is your  
11 supplemental report -- and I'm sorry -- yes, DX 60, which is  
12 your original report, on Page 22.

13 A. Okay. Shall I continue?

14 Q. Yes.

15 A. In Paragraph 73 of my initial expert report, Page 24,  
16 bottom of Page 24, this is the paragraph that reports the  
17 results that I've been trying to remember accurately, and  
18 the third sentence I can just read. "Furthermore, most  
19 participants who were forced to liquidate NGH held exactly  
20 the same RJR and NGH positions that they received in the  
21 spin-off, without having either increased or decreased those  
22 investments." So the correct term is most.

23 Q. Doctor Montgomery, are you aware of academic literature  
24 which has concluded that 401(K) investors tend to be --  
25 strike that.

1           Are you aware of academic literature contending to find  
2   a significant amount of inertia in the behavior of 401(K)  
3   participants?

4   A.    Yes, I am.

5   Q.    Based on the studies and research you have just  
6   testified to, do you have an opinion as to whether the  
7   participants in this Plan have exhibited any degree of  
8   inertia?

9           MR. LEWIS:  Your Honor, objection.  Beyond the  
10  scope of expertise.

11          THE COURT:  Doctor Montgomery, would you step back  
12  out in the hall, please.

13          (The witness left the courtroom.)

14          THE COURT:  Mr. Lewis.

15          MR. LEWIS:  Same objection.  He is not qualified  
16  as an expert in participant behavior in 401(K) plans,  
17  inertia or anything else.  The fact that he just read some  
18  academic literature, it doesn't change the fact that the  
19  Court has not qualified him as an expert -- nor does it  
20  establish him as an expert in that regard.  I could read the  
21  article also, but it doesn't make any me an expert.

22          MR. CHARNES:  He just doesn't read articles, he  
23  did several statistical studies regarding participants'  
24  behavior, and I think it's well within the field of  
25  economics and finance for him to testify about his opinions

1 regarding how they reflect on the -- consistent with the  
2 economics literature that shows participants' inertia.

3 Doctor Biller agreed there was economic literature  
4 that found participants to be extremely -- exhibit extreme  
5 inertia in 401(K) accounts and agreed in his experience he  
6 found that.

7 THE COURT: Then you don't need Doctor  
8 Montgomery's opinion; is that right?

9 MR. CHARNES: Well, I think the difference is,  
10 that Doctor Biller was explaining his experience and Doctor  
11 Montgomery would be testifying about what he found based on  
12 his statistical analysis.

13 THE COURT: He's testifying about what he found on  
14 his statistical analysis of these participants?

15 MR. CHARNES: Yes, sir.

16 THE COURT: But he really is not an expert with  
17 regard to anything else, is he?

18 MR. CHARNES: I think his opinion would be based  
19 on his -- he has an opinion about inertia exhibited by these  
20 participants.

21 THE COURT: Why do you need to get his opinion  
22 about that as long as you have the number?

23 MR. CHARNES: That's fine, Your Honor, I'll move  
24 only.

25 THE COURT: When you get to a convenient stopping

1 place, we'll take our luncheon recess. You let us know when  
2 you get there.

3 MR. CHARNES: I think I just have one or two more  
4 questions, Your Honor.

5 THE COURT: Okay.

6 BY MR. CHARNES:

7 Q. Doctor Montgomery, based on a risk analysis that you  
8 have -- that you performed and to which you just testified,  
9 do you have an opinion about the implications of your  
10 findings for Plaintiff's claims for breach of fiduciary  
11 duty?

12 A. Yes, I do.

13 Q. And what is that?

14 A. My opinion is, that the decision to remove or not to  
15 retain NGH and NA Stocks was to the benefit of participants.  
16 There were no extraordinary returns to be expected from  
17 either stock, so the participants were not giving up any  
18 expected returns beyond which -- beyond those they could  
19 have already attained from other investments in the Plan,  
20 and generally the risk borne by participants declined when  
21 NGH and NA were removed and, therefore, the decision to  
22 remove the stocks didn't raise risk. The combination of not  
23 sacrificing any expected extraordinary returns and not  
24 raising risks, in fact lowered risk, makes this a beneficial  
25 decision for Plan participants, and also a prudent decision.

1 Q. If you would please --

2 MR. LEWIS: May I have a motion to strike on that  
3 one? May I take one second? I'm being passed notes here.  
4 If I could take one second on that, literally.

5 THE COURT: You mean to confer?

6 MR. LEWIS: To confer, yes.

7 THE COURT: Surely.

8 MR. LEWIS: I'll just cross-examine instead, Your  
9 Honor.

10 MR. CHARNES: Now is a convenient time, Your  
11 Honor.

12 THE COURT: Why don't we take our luncheon recess  
13 at this time. Doctor Montgomery, not that you intended to  
14 carry on a conversation with folks on this side of the  
15 courtroom, if you would suppress that desire until a later  
16 time.

17 Let's take a luncheon recess.

18 (Luncheon recess taken from 12:45 p.m. to 2:00  
19 p.m.)

20 BY MR. CHARNES:

21 Q. Doctor Montegomery, if you would please turn to  
22 Defendant's Exhibit 239.

23 A. Okay.

24 Q. What is your third major opinion?

25 A. The third major opinion, as I mentioned before the

1 break, also is that because the removal of NGH and NA cannot  
2 reduce expected returns in the Plan, and it did not -- and  
3 because the removal of NGH and NA did not increase risk,  
4 removing NGH and NA was beneficial to Plan participants and  
5 was not imprudent.

6 Q. And you testified to the basis for that right before  
7 the break for lunch; is that correct?

8 A. That's correct.

9 MR. CHARNES: Your Honor, in the next series of  
10 questions, we'll be referring primarily to Defendant's  
11 binders three, four and five.

12 Doctor Montgomery, if you want to refer to his  
13 expert report, that will be in two. And also be looking at  
14 some point in Plaintiff's binder 11. I can give you  
15 forewarning for that one when we get closer.

16 BY MR. CHARNES:

17 Q. Doctor Montgomery, did Professor Lys and Doctor Biller  
18 both contend that the stock market is not perfectly  
19 efficient and, therefore, investors could have expected to  
20 receive returns on NGH and NA above those as the market as a  
21 whole?

22 THE COURT: Sustained.

23 MR. LEWIS: Objection.

24 BY MR. CHARNES:

25 Q. Doctor Montgomery, do you have an opinion as to whether

1 the stock market is perfectly efficient?

2 A. Well, I don't believe that it is perfectly efficient,  
3 no.

4 Q. Does that opinion impact or undermine your prior  
5 testimony in any way?

6 A. No. I don't think that any of my conclusions depend on  
7 perfect efficiency. The market for NGH and NA Stocks were  
8 generally efficient, and that is one of the bases for my  
9 opinion.

10 Q. Did you hear testimony in this case about certain  
11 anomalies that have been reported in the academic literature  
12 with respect to efficient market hypothesis?

13 A. I did.

14 Q. Do you have an opinion about how that impacts your  
15 testimony, if at all?

16 A. It does not effect my testimony. The two major  
17 anomalies that have been cited by, I believe by Professor  
18 Lys, pertain to post-earnings announcement drift effect, and  
19 something called the accruals and anomaly. I maybe should  
20 just briefly explain. An anomaly in the literature is a  
21 pattern of returns in an association of abnormal returns  
22 with some other factor that appears to be anomalous, and  
23 that it appears to be not in conformity to the market that  
24 are generally expected to be efficient.

25 I think there is extensive literature on both of these



1 topics. Neither of them seem to be at all relevant to  
2 this -- the issues having to do with the removal of NA or  
3 NGH. There is no issue with post-earnings announcement  
4 drift in this case. There is also no assertion that I'm  
5 aware of, that somehow relates to the level of accruals in  
6 NGH or NA's financial statement, and those are the degrees  
7 to which those two anomalies would be relevant, and there is  
8 no relevance that I am aware of.

9 Q. Doctor Montgomery, did Professor Lys cite a study that  
10 he testified in his report -- he opined that stocks with  
11 higher ratings outperform those with lower ratings?

12 A. Yes. He did state a study. It was by Barber and three  
13 coauthors.

14 Q. In your opinion, does that study support the opinion he  
15 gave in this case?

16 A. No. In my opinion, it does not support his opinion.

17 Q. Could you explain that to the Court, please.

18 A. Yes. I think there are at least three, maybe four  
19 reasons that it does not support his opinion. The first is,  
20 that the amount of -- well, let me back up. The study is a  
21 study of analyst ratings and stock returns associated with  
22 strategies of investing that are based on investing in stock  
23 with the highest analyst ratings, and actually selling  
24 short, those stocks with the worst analyst ratings. The  
25 study overall, concludes that the strategy of investing in

1 the highest rated stocks would give investors following that  
2 strategy, about a 4 percent return, 4 percent abnormal  
3 return per year, and I do not believe that a 4 percent  
4 return is anything to do with large returns that NA and NGH  
5 achieved in 2000, and then are part of the claim in this  
6 case.

7 The other important point to make about that case, even  
8 if you accept that the 4 percent is relevant is, that that  
9 case, that paper, rather, says up front, that the result  
10 could not apply to the several hundred companies with the  
11 largest market capitalizations, that they do not find any  
12 discernible effect, any discernible relationship between  
13 analyst ratings and abnormal returns for those top several  
14 hundred companies.

15 Nabisco -- both Nabisco Stocks would be in the category  
16 of the top several hundred companies in market  
17 capitalization and, therefore, the study is not relevant for  
18 either of the Nabisco Stocks.

19 The third point to make is, that the category of stocks  
20 with the highest analyst ratings, actually is the category  
21 with an average rating that were substantially better than  
22 the rating that NA and NGH had during 1999 and early 2000.  
23 So again, it is not relevant to this case.

24 The final point to make is, that that study analyzed  
25 data through 1999, and it indeed found that subject to the

1 qualifications I've mentioned, that there is a positive  
2 relationship between analyst ratings and subsequent stock  
3 returns, and the follow-up study, the same authors looked at  
4 data for 2000 and 2001, and in fact found the opposite  
5 results; more highly rated stocks had a worse return in  
6 2000, 2001, than low rated stocks. So, that shows that this  
7 is not a general phenomenon, that it's very sensitive to the  
8 period in which you are looking and, you know, in reality,  
9 the return -- positive returns that this case is focusing  
10 on, are returns that happened in 2000.

11 So for those reasons, I do not believe that the study  
12 is relevant to anybody's opinion in this case.

13 Q. Doctor Montgomery, did Professor Lys testify that there  
14 was a large body of academic literature documenting, in his  
15 view, the utility of analyst reports in making investment  
16 decisions?

17 MR. LEWIS: Objection.

18 THE COURT: Sustained.

19 BY MR. CHARNES:

20 Q. Doctor Montgomery, did you hear testimony from  
21 Professor Lys regarding a large body of academic literature  
22 related to utility of analyst reports?

23 MR. LEWIS: Objection.

24 THE COURT: Sustained.

1 BY MR. CHARNES:

2 Q. Doctor Montgomery, in your opinion, is there a large  
3 body of academic literature that supports the conclusion  
4 that analyst reports are useful in making investment  
5 decisions?

6 MR. LEWIS: Objection.

7 THE COURT: Would you step out in the hall,  
8 please.

9 (The witness left the courtroom.)

10 MR. LEWIS: He has no expertise in academic  
11 literature. He couldn't even testify that he ever read a  
12 single paper on this issue until he did work in this case on  
13 the issue of analyst reports and recommendations, so I don't  
14 know what his qualification is to talk about the large body  
15 of academic literature, when he never looked at it before  
16 this case.

17 MR. CHARNES: Well, Your Honor, I don't think that  
18 accurately reflects what his testimony is, but the fact of  
19 the matter is, I can lay this foundation, he did review the  
20 literature for this case and that, therefore, he is  
21 qualified to comment on whether -- comment on the size of  
22 the studies that exist as to the value or not of analyst  
23 reports in making investment decisions.

24 Whether he read them before or after his  
25 engagement in this matter is of little relevance to the

1 question, if he's read them now and can testify about them.

2 MR. LEWIS: Well, he's done no systematic study of  
3 this in the past. I don't know that he's any more qualified  
4 than anybody else to testify about what's in the literature.  
5 I mean, it's his opinion as to the literature without a  
6 background in that literature, without ever doing any  
7 empirical studies of it himself. I don't think he has the  
8 background.

9 THE COURT: You think there is some requirement  
10 that he did empirical studies himself?

11 MR. LEWIS: Not necessarily empirical studies  
12 himself, but at least study the literature prior to the  
13 case, at least have some sense of what is out there, what is  
14 not out there, what the literature says overall. If the  
15 standard, I guess is any economist can come in and read  
16 literature and give opinions, then I suppose he's qualified.

17 THE COURT: Why couldn't he do that?

18 MR. LEWIS: Because I think in order to get  
19 context to what you are reading, you need to have some  
20 background in it and some basic knowledge to apply. It is  
21 not just -- he's being asked for a conclusion about what the  
22 whole body of literature concludes or doesn't conclude, and  
23 now the context and background. I don't think he's capable  
24 of doing that.

25 THE COURT: I'm going to allow you to

1 cross-examine him about that. Now, if it's something that  
2 was not in his reports, and it's not a timely opinion,  
3 that's one thing. I think he has established that he has  
4 sufficient experience and expertise generally, to allow him  
5 to review the literature and say what the literature does or  
6 does not say in his opinion.

7 MR. LEWIS: I did check his report -- to Your  
8 Honor's other question, as to whether it was in the report,  
9 the sweeping conclusion that is being asked.

10 MR. CHARNES: I would simply note that Professor  
11 Lys so testified about the body of academic literature,  
12 there is nothing in his report. He did not opine in his  
13 report about the existence of a large body of literature one  
14 way or the other. He cited a couple of studies which Doctor  
15 Montgomery cited in his report and on which he just  
16 testified about. There was no opinion in Professor Lys'  
17 reports regarding a body of literature, even though he did  
18 testify to that.

19 So, I think, you know, existence of the literature  
20 or not is more or less a factual question.

21 THE COURT: You're the one that raised the  
22 question of a large body of literature in the framing of the  
23 question.

24 MR. CHARNES: That was in response to how  
25 Professor Lys testified, and that testimony -- and that

1 testimony was not reflected -- the basis of that opinion was  
2 not reflected in his prior report.

3 THE COURT: Did you object? Did you object to his  
4 prior report?

5 MR. CHARNES: We did not.

6 MR. LEWIS: In looking through his initial report,  
7 Your Honor, we have not found it in there and we're looking  
8 quickly through the supplemental report.

9 THE COURT: Okay.

10 MR. LEWIS: We're not finding it, Your Honor, in  
11 the supplemental report.

12 THE COURT: Can you point that out, Mr. Charnes?

13 MR. CHARNES: I'm sorry.

14 THE COURT: Can you point out in his expert  
15 witness reports where he discusses this?

16 MR. CHARNES: Well, I don't believe he discussed  
17 it in those terms. He did indicate that he reviewed the  
18 literature. This is not -- I don't think it --

19 THE COURT: Show us what you're talking about, and  
20 perhaps I'm confusing this with something else, but did he  
21 not testify in the deposition testimony that Mr. Lewis asked  
22 him about that he was not familiar with that?

23 MR. CHARNES: No. I don't think that is correct.

24 THE COURT: Perhaps I'm confusing that with  
25 something else.

1           MR. CHARNES: Let me read one, DX 60, which is his  
2 initial report, on Page 14, section on analyst reports, he  
3 wrote, I quote --

4           THE COURT: Page what?

5           MR. CHARNES: Page 14 of DX 60.

6           THE COURT: Okay.

7           MR. CHARNES: In Paragraph 34 at the top of the  
8 page of he wrote, second sentence, "economic literature  
9 indicates that any information from analyst opinions, like  
10 any other public information, would have been rapidly  
11 incorporated into market prices for NGH and NA." And in  
12 this report, and more so in the rebuttal report, he  
13 specifically discusses references to the articles that in  
14 the academic literature that Professor Lys relied on.

15           In his deposition, I do not believe it is correct  
16 to say that he was unfamiliar with that literature on the  
17 two anomalies. During voir dire what Mr. Lewis went over  
18 were his knowledge of economic literature on the two  
19 so-called anomalies in the efficient market hypothesis. I  
20 do not recall him talking about literature regarding analyst  
21 reports in general, and I think what he would testify to is,  
22 that he reviewed the academic literature before arriving at  
23 his opinions, and identified those articles that related to  
24 analyst reports and, therefore, is familiar with the extent  
25 of the academic literature on analyst reports.



1 THE COURT: Why don't you lay that foundation.

2 MR. CHARNES: Okay. Yes, sir.

3 THE COURT: And you may object.

4 MR. LEWIS: Thank you, Your Honor.

5 BY MR. CHARNES:

6 Q. Doctor Montgomery, during the course of developing your  
7 opinion in this case, did you review academic literature  
8 relating to the value of analyst reports in financial and  
9 investment decisions?

10 A. Yes, I did.

11 Q. You did that --

12 THE COURT: The question is, when.

13 THE WITNESS: The question is when?

14 THE COURT: That's my question.

15 BY MR. CHARNES:

16 Q. That's the more important question.

17 A. I reviewed -- well, I'm not sure I remember exactly. I  
18 know I reviewed the Barber paper cited by Professor Lys  
19 before I wrote my first report. I don't recall whether I  
20 reviewed it then, relative to later. It is just a little  
21 bit difficult to recall the timing.

22 Q. I guess the question is, Doctor Montgomery, did you  
23 generally survey the economic literature in an attempt to  
24 identify academic papers discussing the value of analyst  
25 reports before finalizing your supplemental opinion in this

1 case?

2 A. I made an effort to identify whether there were any  
3 papers that would be relevant to the opinion. I can't find  
4 any.

5 Q. Apart from the papers that Professor Lys cited, you did  
6 not find any additional papers discussing analyst reports?

7 A. There are certainly other articles involving analyst  
8 reports, but I don't believe that any of them specifically  
9 bear on the issue at hand.

10 Q. By the issue at hand, what are you referring to?

11 A. Well, you know, the -- I don't think I did an  
12 exhaustive search for articles related to analyst reports  
13 and the association of analyst reports and returns. I  
14 looked at the -- looked at some articles. Obviously I  
15 looked at the Barber article, and I looked at some others,  
16 and none of them provided evidence that they would have been  
17 useful in the issues in this case in terms of helping to  
18 predict any extraordinary returns in NGH and NA. It's a  
19 little difficult for me to say how exhaustive the search  
20 was.

21 THE COURT: I sustain the objection with regard to  
22 the body of literature generally. You have elicited his  
23 position with regard to the Barber article and what if any  
24 significance it had with regard to the issues in this  
25 matter.

1 MR. CHARNES: Thank you, Your Honor.

2 BY MR. CHARNES:

3 Q. Doctor Montgomery, did you perform any analysis of  
4 stocks generally, for the period of 1999 and 2000, with  
5 ratings similar to those -- analyst ratings similar to those  
6 of NGH and NA to determine how they performed?

7 A. Yes, I did. I did an analysis of large CAP stocks,  
8 those in the S&P 500 Index in 1999/2000, and looked at how  
9 stocks were different -- at different levels of rating  
10 performance during those two years.

11 Q. What were your conclusions, based on the study that you  
12 performed?

13 A. My conclusion, and this is shown in the exhibits in my  
14 report, my initial expert report was, that there was no  
15 evidence -- evident association between returns and analyst  
16 ratings between those stocks and those earnings.

17 Q. Did you, with reference to DX 60, which is your  
18 additional analyst report --

19 A. Expert.

20 Q. Could you please refer the Court to the results of that  
21 study.

22 A. The results of the study are shown in Exhibit 11 to my  
23 initial report, Defendant's Exhibit 60, probably about three  
24 quarters of the way through the entire exhibit. Exhibit 11  
25 is a four page exhibit.

1 Q. Is Exhibit 11 to your report discussed in the text of  
2 your report beginning at Paragraph 28 on Page 11 -- I'm  
3 sorry, Paragraph 32 on Page 13?

4 A. Yes, it is. In fact, Paragraph 32 is the primary  
5 discussion of the results.

6 Q. Could you, Doctor Montgomery, please read Paragraph 32  
7 for the record.

8 A. Okay. "We performed our own analysis of the return of  
9 stocks with similar ratings to NGH and NA. Exhibit 11 shows  
10 the performance of stocks in the Standard and Poor's 500  
11 Index in 1999 and 2000, comparing those with similar ratings  
12 to NGH and NA to other stocks. We separated the members of  
13 the S&P 500 Index into quintiles based on the strength of  
14 their analyst ratings as of the beginning of 1999 and 2000,  
15 and calculated their returns over the next 12 months. We  
16 defined the strength of analysts' ratings in terms of both  
17 the average ratings for a stock, as well as the percentage  
18 of ratings for a stock that were "buys." During 1999 and  
19 2000, stocks with ratings similar to those for NGH and NA  
20 did not tend to exhibit extraordinary returns over the next  
21 12 months. The median returns for stocks with their ratings  
22 range from negative -5.6 percent to 17.8 percent, compared  
23 with median returns for all stocks ranging from 1.2 percent  
24 to 11.9 percent. We also did not find any evidence that  
25 stocks with more favorable analyst ratings delivered better

1 investment returns than stocks with less favorable ratings."

2 Q. Doctor Montgomery, in his expert report, did Professor  
3 Lys conduct an econometric analysis addressing the value of  
4 analyst reports?

5 A. Yes. He provided -- did an econometric study in his  
6 supplemental report and then another one including a  
7 correction in his initial.

8 Q. Do you have an opinion with respect to the validity of  
9 his analysis regarding the value of analyst reports?

10 MR. LEWIS: Objection. If I can explain.

11 THE COURT: Would you step back out in the hall.

12 (The witness left the courtroom.)

13 THE COURT: Which analysis are you referring to?

14 MR. CHARNES: I'm referring to the analysis both  
15 done in his supplemental report and in the addendum  
16 correction, it is called, to that report.

17 MR. LEWIS: That would be the analysis that  
18 Professor Lys testified he was not relying on and giving his  
19 opinions at trial in this case. We have that whole going  
20 back and forth, and for awhile, you let Mr. Taylor question  
21 him about it, and I think eventually curtailed it, Your  
22 Honor, and I believe that since Professor Lys is not basing  
23 any of his opinions on that analysis, I don't see the  
24 relevance of the question.

25 MR. CHARNES: I think we can impeach Professor Lys

1 based on any work he did in the case. He provided two  
2 analyst reports -- excuse me, two expert reports that  
3 provided this progression analysis in two different forms,  
4 and I think it's fair game for Doctor Montgomery to testify  
5 whether he thinks those results are fair and up to  
6 scientific standards or not. I think if they are not and  
7 the Court is convinced by Doctor Montgomery that they are  
8 not, I think that impacts Doctor Lys' credibility as a  
9 witness and, therefore, is relevant.

10 THE COURT: Even though he has disavowed them  
11 himself?

12 MR. CHARNES: I think disavow is not quite the  
13 word. He did not rely on them on the witness stand. I  
14 don't think he disavowed them. I think the fact that he put  
15 them forth in his expert report that were duly served on  
16 opposing counsel in the case, and opposing party, makes them  
17 fair game for use at trial, and one of the reasons  
18 potentially why he's not relying on them, go to his  
19 credibility and trustworthiness as an expert.

20 THE COURT: I think at this point it is needless  
21 to do that. I think it's a waste of time, and I will  
22 sustain the objection.

23 BY MR. CHARNES:

24 Q. Doctor Montgomery, what if any research did you do to  
25 identify analyst reports in addressing the NGH and NA Stocks

1 during the period of 1999 and early 2000?

2 A. I did several different things. First of all, I looked  
3 at the database on IBES that contains, among other  
4 information, the data on analyst ratings of stocks from  
5 strong buy, strong sell, and I evaluated those ratings for  
6 NA and NGH. In particular, in response to the Plaintiff's  
7 expert opinions on the subject, I also reviewed analyst  
8 reports that I received from counsel, and I also obtained  
9 any other reports that I could obtain from public databases,  
10 and I read all of those reports. Those are the primary ways  
11 that I obtained information and analyst reports regarding  
12 NGH and NA.

13 Q. To the best of your knowledge, did you review all of  
14 the analyst reports that were produced by the Plaintiff or  
15 that were relied on by any of the Plaintiff's experts?

16 A. Yes. To the best of my knowledge, I did.

17 Q. Based on your review of all the analyst reports that  
18 you testified that you had in your possession, was there  
19 any --

20 THE COURT: And I hate to spend more time on this,  
21 but I think you need to go through what they were. I think  
22 this -- I don't know as I sit here what he has reviewed.

23 MR. CHARNES: You want him to identify the  
24 particular analyst reports?

25 THE COURT: Yes.

1 BY MR. CHARNES:

2 Q. Doctor Montgomery, if you would please turn to  
3 Defendant's Exhibit 60, which is your initial report in this  
4 case.

5 A. Yes.

6 Q. In particular, I would like to refer you to Exhibit 2  
7 to your report.

8 A. Yes. This is the exhibit of materials considered.

9 Q. And in Exhibit 2 to your report, did you list by name  
10 and date, each of the analyst reports that you reviewed as  
11 part of this -- your work on this case?

12 A. Well, this is a list of all of the reports that I had  
13 reviewed, as complete as I felt I could make it. I have  
14 other reports that I have obtained and reviewed by the date  
15 of this initial report. I may have received others  
16 presumably from counsel after that, but these were all the  
17 ones that I had at this time.

18 Q. Would you please turn to Defendant's Exhibit 64, your  
19 supplemental report. Are there any additional -- in Exhibit  
20 1 to your supplemental report, DX 64, are there any  
21 additional analyst reports that you obtained after your  
22 initial report but prior to finalizing your supplemental  
23 report?

24 A. No. There are none. There are none listed here so,  
25 therefore, there are none.



1 Q. Was this analyst information that you obtained?

2 A. I don't believe there was any additional information.  
3 Now it says in this list that there was additional IBES  
4 inspection. I can't recall exactly which IBES information  
5 we got for the supplemental report that we didn't already  
6 have for the initial, and I'm just not sure about.

7 Q. If I understand your testimony, you believe that the  
8 analyst reports that you reviewed listed in the -- excuse  
9 me, listed in Exhibit 2 to your initial report; is that  
10 correct?

11 A. Yes.

12 Q. And based on your review of those reports that you  
13 listed in that Exhibit 2 to your expert report, do you have  
14 an opinion as to whether analysts were expecting or  
15 forecasting the returns on NGH and NA that actually occurred  
16 after January 31st, 2000?

17 A. Yes. I do have an opinion about that.

18 Q. What is your opinion?

19 A. My opinion is, that they were not forecasting the scope  
20 of the returns that NGH and NA had in 2000. After  
21 January 31st, 2000, none of them were expecting the chain of  
22 events starting with the bid by Carl Icahn that led to the  
23 large rise in NGH and NA.

24 Q. Are all of the analyst reports on NA and NGH predicting  
25 appreciation of stock prices of those stocks?

1 A. No. I don't believe so. Some, I think, had price  
2 targets that implied some appreciation, others were more  
3 pessimistic.

4 Q. If you would please turn to DX 301.

5 A. I forgot the number.

6 Q. 301. If you would please turn to Page 24 of  
7 Defendant's Exhibit 301, 24 and 25. Are you there?

8 A. I'm there.

9 Q. And were you present in the courtroom when Professor  
10 Lys testified about these two figures from his report?

11 A. Yes, I was.

12 Q. And, did Professor Lys use figure four and figure five  
13 on Pages 24 and 25, to present his opinion that analysts  
14 were increasingly more positive about the Nabisco Stocks as  
15 time passed in 1999?

16 A. That is my recollection, yes.

17 Q. Doctor Montgomery, have you determined whether in  
18 putting together figure four and figure five, whether  
19 Professor Lys included all published analyst recommendations  
20 or just those recommendations that had been issued within  
21 the last month?

22 A. Yes. I have determined that these are all published  
23 recommendations. These are basically all recommendations  
24 that would have been in the IBES database as of any  
25 particular month, and that would include recommendations

1 that had been issued months, many months before.

2 Q. And did Professor Lys testify that when he performed  
3 his regression analysis --

4 THE COURT: Sustained. I'm not going to let one  
5 witness recall what another witness testified to. That's  
6 for the finder of fact to recall.

7 MR. CHARNES: I'll rephrase the question.

8 BY MR. CHARNES:

9 Q. Doctor Montgomery, did you review Professor Lys'  
10 addendum -- strike that.

11 Doctor Montgomery, did you review the addendum  
12 correction to Professor Lys' supplemental report which is  
13 Defendant's Exhibit 303?

14 A. Yes, I did.

15 Q. In his addendum correction in the regression analysis  
16 he performed therein, did Professor Lys remove from his  
17 analysis reports that were older -- analyst recommendations  
18 that were older than one month?

19 MR. LEWIS: Objection, Your Honor. We're getting  
20 back into this correction regression analysis, which was not  
21 the basis of Professor Lys' testimony.

22 THE COURT: Doctor Montgomery, would you --

23 (The witness left the courtroom.)

24 MR. LEWIS: Perhaps there is some connection I'm  
25 missing, but it seems like we're getting back to the

1 regression analysis which Professor Lys is not relying on.  
2 If there is something I'm missing, I will certainly listen,  
3 and perhaps withdraw the objection.

4 MR. CHARNES: I'm not seeking to go back to the  
5 regression analysis, but I think Professor Lys did things  
6 that are inconsistent. In putting together figure four and  
7 figure five, upon which he testified in this courtroom, he  
8 included all, as Doctor Montgomery just testified, he  
9 included all previous analyst reports that were still in  
10 existence as of a particular day. When Professor Lys did  
11 his regression analysis, however, he excluded, and I believe  
12 he testified about this on cross-examination, he excluded  
13 what were referred to as stale reports, that is reports that  
14 were older than one month, and he testified that he did this  
15 to increase the accuracy of his regression analysis.

16 What Doctor Montgomery will testify that he  
17 revised, Professor Lys' figure four and figure five to  
18 remove the reports that Professor Lys in his addendum and  
19 corrections concluded were stale and he will testify about  
20 what these tables look like if you remove the so-called  
21 stale reports, and give his opinion about what that shows  
22 about the trend in the analyst reports if you remove the  
23 stale reports. That's where we're going with this.

24 MR. LEWIS: And although I think we're comparing  
25 apples and orange when you are talking about what one might

1 do to do a regression analysis for statistical significance  
2 and doing what Professor Lys did in four and five, I can  
3 cross-examine him about that, so I will withdrawal the  
4 objection at this time.

5 BY MR. CHARNES:

6 Q. Doctor Montgomery, referring you back to -- I'm sorry,  
7 let me strike that.

8 In his addendum and correction, did Professor Lys, in  
9 the regression analysis of figure one, remove analyst  
10 recommendations from his analysis that were older than one  
11 month?

12 A. Yes, he did. And in Paragraph 2, part B of this  
13 addendum, he makes that statement.

14 Q. Would you read that for the record.

15 A. "For each month, I used only recommendations that were  
16 released in that month by individual analysts." Then there  
17 is a long passage in parentheses. "(The analysis in the  
18 supplemental report was based on IBES consensus  
19 recommendations and, as such, was based on the average  
20 recommendations and the changes thereof as reported by IBES.  
21 Because of the way in which IBES aggregates its data, the  
22 average analyst recommendation reported by IBES includes  
23 carryover recommendations from previous months.)"

24 Q. Thank you. Now, with respect to figures four and five  
25 in his initial report, did you determine whether Professor

1 Lys similarly excluded -- strike that.

2 Did you determine whether Professor Lys similarly used  
3 recommendations that were released in that month?

4 A. No. He did not do that. He used all recommendations.

5 Q. Did you revise Professor Lys' figures for four and five  
6 in order to restrict the data in that chart to analyst  
7 recommendations issued in that month?

8 A. Yes, I did. I took the restricted data from the data  
9 set that Professor Lys used in these regressions, and  
10 reconstructed a version of the charts with one difference  
11 that I can explain, based on non-stale recommendations that  
12 is the recommendations that actually are dated.

13 Q. Would you like to explain the difference?

14 A. The difference is, the charts that I prepared, there  
15 only are at most two, maybe three recommendations, if I can  
16 recall correctly, without looking at the chart, only two or  
17 maybe three recommendations released in a particular month,  
18 so it didn't really make sense to go at the scale like  
19 Professor Lys. Professor Lys' exhibits goes from zero to a  
20 hundred percent, so instead, I have the scale just one, two,  
21 three, whatever the number the analyst ratings there are.

22 Q. If you please turn to Defendant's Exhibit 298.

23 THE COURT: That's number what?

24 MR. CHARNES: Twenty-nine.

25

1 BY MR. CHARNES:

2 Q. Doctor Montgomery, what is Defendant's Exhibit 298?

3 A. This 298 is a reconstruction of the tables as four and  
4 five, if I recall correctly, from Professor Lys' original  
5 exhibit, but using the current recommendations, that is the  
6 recommendations released that month, in line with the  
7 approach Professor Lys used in his addendum, and what this  
8 shows is, for each month, if you want to look at the first  
9 page, the first page is for NGH, it starts -- actually, it  
10 starts before Professor Lys' exhibit did. It starts in  
11 January '99, so it would actually be starting with RJR  
12 Nabisco, and then in June '99, RJR Nabisco becomes NGH.

13 It shows the fresh recommendations, that is the  
14 recommendations that are actually released in the month  
15 showing the graph, and it shows whether they're buy, which  
16 is the blue; hold, which would be red; or sell, there are no  
17 sell, but they would be yellow. And it shows the number of  
18 recommendations. If a particular analyst had more than one  
19 recommendation in a month, it would show the latest one in  
20 that month and that happens once or twice.

21 Q. And with respect to the first page, which as I  
22 understand it relates to NGH, what if any conclusions or  
23 opinions do you have with respect to trend analyst  
24 recommendations with respect to NGH?

25 A. My opinion would be that if you take the approach of

1 only using the fresh recommendations, there is no clear  
2 trend in analyst recommendations. Arguably, if you look at  
3 September to October in 1999, there may be a negative trend  
4 because you're going from one buy in September to a buy and  
5 hold in October 1999.

6 Q. If you please turn to the second page of DX 298. What  
7 is this page?

8 A. This is the same exercise, but for NA instead of NGH.  
9 It shows the number for each month of the number of fresh  
10 recommendations issued for NA in each month, and by the way,  
11 when there is nothing for a particular month, that means  
12 there were no fresh recommendations. Perhaps just to go  
13 back to the previous chart, there were no fresh  
14 recommendations for NGH after October 1999.

15 Any way, back to the second page, it shows the same  
16 information for NA.

17 Q. And what if any opinions do you have with respect to  
18 NA, based on the second page of this exhibit?

19 A. Well, I don't think that one -- there isn't any clear  
20 trend in recommendations, if you look at this chart.

21 Q. Doctor Montgomery, did you perform any analysis to  
22 determine whether spin-offs, including spin-offs that are  
23 positively touted by company management analysts, invariably  
24 increase shareholder value in subsequent periods of time?

25 A. Well, that follows from the presumption and the



1 demonstration of the fact that the -- that records for  
2 stocks like NGH and NA at least are efficient.

3 I also did have my staff research other spin-offs, and  
4 look for examples of spin-offs that although good things  
5 were generally expected from the companies involved in the  
6 spin-offs, the stocks of those spin-offs in fact didn't turn  
7 out well, and we did find a number of examples where  
8 although the spin-offs were touted, the stocks did not  
9 perform well.

10 Q. Would you please turn to Defendant's Exhibit 280, which  
11 is in notebook four. Do you have that document, Doctor  
12 Montgomery?

13 A. I do.

14 Q. What is Defendant's Exhibit 280?

15 A. This is a summary of some of the information from the  
16 analysis of spin-offs that I reported in my initial expert  
17 report.

18 It shows the stock return detail for three spin-offs  
19 that occurred before the spin-off by RJR Nabisco of RJ  
20 Reynolds Tobacco, and they are -- these three spin-offs are  
21 the spin-off by Kimberly Clark of a company that is  
22 difficult to pronounce, Schwitser Maunduih and the spin-off  
23 of Fortune Brands by the Gallagher Group and the spin-off by  
24 Campbell Soup company of Vlassic Foods International.

25 The table shows some of the press coverage of the

1 spin-offs to show that positive things were expected from  
2 the spin-off and the spin-off was expected to be positive  
3 for the companies involved, and then it shows the stock  
4 returns relative to the market for the 12 months following  
5 the spin-off, for the period up through June 14, '99, when  
6 the RJR Nabisco spin-off occurred, and through -- and also  
7 the returns through January 31st, 2000, when the NGH and NA  
8 were removed from the CIP.

9 Q. Doctor Montgomery, is the information contained in  
10 Defendants Exhibit 280, also contained in Exhibit 12 to DX  
11 61, which is the corrections to your initial report?

12 A. Yes, it is.

13 Q. Would using Defendant's Exhibit 280 assist your  
14 testimony today?

15 A. Yes, it would.

16 Q. Will you please turn to the first page of 280. What  
17 does your research show with respect to the spin-off  
18 reflected on that page?

19 A. This first page is about the spin-off by Kimberly Clark  
20 of Schwitzer. Schwitzer was a company -- Kimberly Clark, of  
21 course, is a large paper goods manufacturer and marketer.  
22 Schwitzer was a subsidiary of Kimberly Clark, whose main  
23 business was cigarette paper, and there were, of course,  
24 concerns about tobacco liabilities. The quote that I have  
25 in this, which are all from Wall Street Journal articles,

1 talk about the desire of Kimberly Clark to have the market  
2 view it as a maker of consumer and healthcare products and  
3 not as a supplier to the tobacco industry.

4 So, you know, it also talks about the -- the third  
5 quote talks about the fact that investors might view this  
6 positively, that they could have their cake and eat it, too,  
7 is how the quote reads.

8 At any rate, the spin-off occurred in 1995. In the 12  
9 months following the spin-off, there were some positive  
10 returns. Kimberly Clark had a 3 percent return relative to  
11 the market. Schwitser had a 19 percent. There was actually  
12 positive returns; however, if you look at it from the  
13 standpoint of sitting on June 14th, 1999 when the spin-off  
14 of RJR Tobacco occurred, at that point, Kimberly Clark had  
15 had a 12 percent negative return relative to the market, so  
16 the stock had underperformed the market, and Schwitser had a  
17 negative 65 percent return relative to the market, so it had  
18 dramatically underperformed the market, and the same basic  
19 conclusion results if you look at the returns through  
20 January 31st, 2000.

21 Q. If you please turn to the second page of DX 280, and  
22 explain to the Court what your research showed with respect  
23 to this spin-off.

24 A. This spin-off is the spin-off by Fortune Brands. Well,  
25 the company was actually called American Brands until it

1 undertook the spin-off. The spin-off by American Brands of  
2 a company called the Gallagher Group, and the Gallagher  
3 Group was the UK tobacco operation of American Brands.  
4 American Brands had previously disposed of its U.S.  
5 cigarette operations, and the Wall Street Journal quotes in  
6 this article -- talks about the American Brands desire to  
7 disassociate itself more fully in the public eye and  
8 investors' eye from the tobacco business. So this is  
9 another tobacco related spin-off. Actually, you can see in  
10 the third quote, that American Brands Stock reacted on the  
11 day of the spin-off by raising 8.1 percent on the news of  
12 the spin-off, so as you would expect with an efficient  
13 market, there was an immediate reaction to it.

14 In the 12 months after the spin-off, however, the  
15 group -- the stock of Fortune Brands, which is what American  
16 Brands had been renamed, underperformed the market by  
17 11 percent, and the Gallagher Group also underperformed the  
18 market by 6 percent, and the underperformance of Fortune  
19 Brands continued through June 14, 1999, and more  
20 dramatically through January 31st, 2000. Gallagher Group  
21 performed a little better to June 14, 1999, but also had  
22 dramatically underperformed by January 31st, 2000.

23 Q. If you please turn to the third page of this exhibit  
24 and please testify about what your research showed regarding  
25 the Campbell Soup/Vlassic spin-off.

1 A. Yes. The Campbell Soup Company spun off a number of  
2 diverse number of food businesses into a company called  
3 Vlassic, named after the pickle part of the business. And,  
4 the quote that I have here talks about how analysts were  
5 encouraged by some of the details of the spin-off.

6 There is an upgrade by the Goldman Sacks analyst, the  
7 Bear Sterns analyst talks about how the new Campbell's has  
8 become the Cadillac of the food business and should command  
9 a higher multiple, that is a higher price relative to its  
10 earnings. That notwithstanding, if you look at the returns  
11 for these companies, Campbell's Soup in the 12 months  
12 following the announcement of the spin-off, underperformed  
13 the market by 5 percent. Vlassic Foods in the 12 months  
14 following the spin-off, underperformed the market by  
15 57 percent, and that both companies also substantially  
16 underperformed the market in the period up to June 14th,  
17 1999, and the period up to January 31st, 2000.

18 Q. Doctor Montgomery, during Mr. Altman's testimony, did  
19 you hear reference to form 11K with respect to the Vlassic  
20 Foods 401(K) plan after the spin-off?

21 A. Yes, I did.

22 Q. Did Vlassic Foods keep frozen Campbell's Stock in the  
23 plan afterwards?

24 A. That's what I recall the testimony being, yes.

25 Q. And based on this page, Page 3 of this exhibit, was

1 that a good -- did that achieve good results or poor results  
2 for the participants in that plan?

3 MR. LEWIS: Objection.

4 THE COURT: And your --

5 MR. LEWIS: Objection is ambiguous.

6 THE COURT: Overruled.

7 MR. LEWIS: Because of the time, Your Honor.

8 THE COURT: You may answer.

9 THE WITNESS: Well, the returns on this chart for  
10 Campbell's Soup are all negative relative to the market and  
11 so, therefore, you know, obviously the participants who  
12 invested in Campbell's Soup would have been off investing in  
13 a diversified stock fund.

14 Q. Now, Doctor Montgomery, you did not perform a  
15 statistically valid sample of all spin-offs prior to  
16 June 14, 1999, is that correct?

17 A. That's correct.

18 Q. What was the reason for your looking at these  
19 spin-offs?

20 A. The reason was to provide examples that contradicted  
21 the -- you know, assertions that I felt that the Plaintiff  
22 was making in the case and I believe also the Plaintiff's  
23 experts that --

24 THE COURT: Sustained in the way that is being  
25 expressed.

1 THE WITNESS: Okay. May I try again?

2 THE COURT: You may.

3 THE WITNESS: I wanted to provide examples that  
4 contradicted the notion that spin-offs invariably are  
5 beneficial for stock, for stock prices and stock returns.

6 BY MR. CHARNES:

7 Q. If you please turn to Defendant's Exhibit 242. What is  
8 this document, Doctor Montgomery?

9 A. This is another summary of information that is taken  
10 from my initial expert report, and this relates to the three  
11 spin-offs we've just been talking about, and one additional  
12 spin-off, and that's the spin-off by General Motors  
13 Corporation, Adelphi Corporation, and the exhibit shows the  
14 analyst ratings one month after the announcement or the  
15 actual spin-off, and the analyst ratings for the eight  
16 stocks involved in these spin-offs and also the returns over  
17 the same periods that previous exhibit showed.

18 Q. And does Defendant's Exhibit 242 include information  
19 that's also contained in Exhibit 13 to your initial report,  
20 which is DX 60?

21 A. I'll just verify the number, but I believe that's  
22 correct. Yes, that's correct, Exhibit 13.

23 Q. Would use of Defendant's Exhibit 242, assist your  
24 testimony today?

25 A. Yes, it would.

1 Q. What if any opinion do you have -- have you arrived at  
2 based on Defendant's Exhibit 242?

3 A. Well, my opinion is, that these are four examples of  
4 companies where there is a mix of buy ratings and hold  
5 ratings by analysts, and almost no sell ratings. I believe  
6 there are 6 percent of the ratings for Campbell's Soup  
7 Company, that's presumably one rating was a sell or  
8 underperform, but the rest of the ratings for all of these  
9 eight companies were either hold or buy, and despite those  
10 evidently positive ratings, the returns were generally  
11 disappointing.

12 Q. Doctor Montgomery, in his expert report, did Professor  
13 Lys list two articles in support of his opinion that  
14 spin-offs generally result in increases in firm values?

15 A. Yes, he did.

16 Q. Did you review those two articles?

17 A. Yes, I did.

18 Q. Do you have an opinion as to whether those articles  
19 support Professor Lys' opinion?

20 A. Yes, I do have an opinion. I don't believe they  
21 support the opinion that there should have been -- that  
22 investors should have expected some future positive return  
23 to the stock, as the stocks would, in some delayed fashion  
24 somehow reflected the benefits of the spin-off. Both of  
25 those articles look at the behavior of stocks around the



1 time of the spin-off, not at some future time after the  
2 spin-off.

3 Q. Did the two articles that Professor Lys cited contain  
4 information about a period of time during which there is a  
5 positive -- strike that.

6 Did the two articles on which Professor Lys cited,  
7 report a period of time during which there is a price  
8 reaction to announced spin-offs?

9 A. Yes, they did. Both -- well, they looked at somewhat  
10 different reactions. One of the articles looked at really a  
11 typical -- typical in the financial economics literature,  
12 looked at a window of a price reaction of, I think about  
13 three days around the announcement of the spin-off, which is  
14 the time you -- as much time as you would expect would be  
15 needed for the market to reflect the new information that is  
16 embodied in the announcement of the spin-off.

17 The other article looked at the movement in the stock  
18 in the year prior to the actual spin-off, which might have  
19 been the time the market first became aware that the  
20 spin-off was going to happen, and the stock in the year of  
21 the spin-off.

22 Q. Doctor Montgomery, did you do any analysis to determine  
23 whether the Nabisco Stocks were likely to rise in price in  
24 the year 2000, simply because they declined significantly in  
25 the year 1999?

1 A. I did do some analysis to on that, that subject, yes.

2 Q. What is your opinion?

3 A. Well, my opinion is, that it follows from the -- all  
4 the reasons I cited earlier about no reason to expect  
5 extraordinary returns based on public information.

6 Moreover, I performed some additional statistical analysis  
7 in my expert report to demonstrate, to test that fact and  
8 also to demonstrate that it is true.

9 Q. What's true, Doctor?

10 A. It is true that there is no tendency of stocks that  
11 have fallen by a significant amount, by the amount that NGH  
12 and NA fell in 1999, to rise at all after that decline, much  
13 less to actually recover the amount of the decline that they  
14 had fallen by or as even to rise as much as NA or NGH rose.

15 Q. Can you please describe what work or analysis you  
16 conducted.

17 A. It might help to refer to my expert report.

18 Q. Sure.

19 A. Which is -- exhibit?

20 Q. Your expert report is Exhibit 60.

21 A. My expert report is Exhibit 60.

22 Q. If you want to also refer to Defendant's Exhibit 243,  
23 which is the demonstrative exhibit, I think Ms. Winchester  
24 might have that.

25 A. I don't have it here.

1 THE COURT: What was the exhibit in 60?

2 THE WITNESS: Exhibit 14, Your Honor, which is a  
3 two page exhibit.

4 BY MR. CHARNES:

5 Q. With reference to your either Defendant's Exhibit 43 or  
6 your expert report or both, could you please describe the  
7 analysis that you conducted in your conclusions.

8 A. Yes. The analysis took as a sample of stock, all of  
9 the stocks that were members of the S&P 500 Index, which is  
10 obviously 500 stocks at the time, over 1999 through 2004.  
11 For each of those stocks, we looked at the stock price  
12 returns over the course of each of those years, and we  
13 identified each time a stock declined by either -- by two  
14 different amounts, either by 60 percent or by 29 percent.

15 It might be easiest to look at the DX 243. 60 percent  
16 is the -- was the drop in -- the amount that NGH Stock  
17 dropped between June 14, 1999 and January 31st, 2000. So,  
18 the first exhibit looks at what happens when the -- all the  
19 stocks in the S&P 500 had a drop of at least 60 percent.

20 Just might mention parenthetically, that RJR Nabisco  
21 was a member of the S&P 500, and then after the spin-off,  
22 NGH became a member of the S&P 500 Index. The graph is a  
23 bar graph showing the distribution of returns of all of the  
24 stocks that had -- every time -- every episode stocks had of  
25 a 60 percent price drop and what the returns were in the one

1 year, that is 250 trading days after that episode, the 60  
2 percent drop. There were -- as one of the green boxes  
3 indicate, there were 326 total episodes of stock with a  
4 60 percent drop. The bar -- the left most bar indicates  
5 that 170 of those episodes, which is more than half, the 170  
6 of those episodes have a 60 percent drop, were followed by a  
7 subsequent drop of some magnitude in the year following the  
8 initial 60 percent drop. So less than half of the companies  
9 had actually a positive return after suffering the  
10 60 percent drop.

11 Then the next three bars to the right show groups of  
12 stock that had positive returns of varying magnitudes.  
13 Seventy stocks had positive returns from zero to 41 percent.  
14 Thirty stocks had increases from 41 to 82 percent.  
15 Thirty-six stocks had increases from 82 to 150 percent. If  
16 you put all of those together and look at that first green  
17 box, 306 of 326 times, the stock did not have an increase of  
18 at least 150 percent.

19 Now, the significance of the 150 percent is, that's in  
20 the increase that stock needs to fully recover from the  
21 60 percent drop. So, 306 of 326 times, the stock did not  
22 fully recover from its drop.

23 Then there are another 14 times where a stock had  
24 between 150 and 247 percent increase. The significance of  
25 247 percent apart from being a big number is, that that's

1 the increase that NGH had from January 31st, 2000 to  
2 December 11, 2000, so out of 326 total episodes of the  
3 60 percent drop, 320 did not manage to have an increase as  
4 high as the increase of NGH and only six had an increase  
5 higher than NGH's.

6 If you want to turn to the next page. The next page  
7 performs essentially the same analysis, but the only  
8 difference is, that instead of identifying a 60 percent  
9 drop, we identified every episode of a 29 percent or greater  
10 drop, and a 29 percent drop is the size of the decline of NA  
11 Stock price from June 14th, 1999 to January 31st of 2000.  
12 So there -- and there are, as the green boxes show, there is  
13 1,693 total episodes. Obviously it is a smaller drop, so  
14 there are more episodes. Of that, of the 1,693, 719, that's  
15 the bar to the left, 719 of those drops were not -- were  
16 followed by a negative -- additional negative stock price  
17 performance, so by an additional claim.

18 The only -- another 616 did not have an increase  
19 as high as 41 percent. Forty-one percent is the amount of  
20 increase you would have to have to get fully recovered from  
21 the 29 percent drop, to get you back to even. So out of  
22 1,693 episodes with a 29 percent drop, 1,335 were not  
23 followed by full recovery. Another 248 had an increase of  
24 41, 82 percent. 82 percent is the actual increase in NA  
25 from January 31st, 2000 through December 11, 2000.

1           So, all in all, out of the 1,693 episodes at the  
2 29 percent drop, like the drop for NA, 1,583 of those  
3 episodes were followed by a return less than the return NA  
4 actually had.

5 Q.    Doctor Montgomery, based on Defendant's Exhibit 243,  
6 the two pages that you have described, what is your opinion  
7 with respect to the stock, the likelihood of stock price  
8 performance of NGH or NA following January 31st, 2000?

9 A.    Well, I think this demonstrates the larger point, that  
10 there are -- just because the stock had a large negative  
11 return, that's public information, and there is no reason,  
12 based on that fact, that the stock had had a large return,  
13 negative return to expect that its return would be anything  
14 out of the ordinary in a subsequent period. The mere fact  
15 that the stock is dropping does not imply that it's going to  
16 increase in the future. A future drop is quite likely.

17 Q.    Doctor Montgomery, do you have an opinion with respect  
18 to whether the stock price appreciation for NGH and NA that  
19 began in March of 2000 was predictable before January 31st,  
20 2000, based on factors in the marketplace?

21 A.    Yes, I do have an opinion on that.

22 Q.    What is that opinion?

23 A.    My opinion is, that it was not predictable.

24 Q.    I would like to start with a little background. Did  
25 you research performance of the NGH and NA Stock prices

1 during the period from June 14, 1999 to December 11, 2000?

2 A. Yes, I did.

3 Q. How did you obtain the data with respect to the two  
4 stock prices during that period?

5 A. My source for data on those two stock prices was Facts  
6 Research Systems, which is a service that NERA subscribes to  
7 and is a widely used service among investment professionals  
8 for obtaining stock price and other financial information.

9 Q. I would like to refer you to Defendant's Exhibit 267,  
10 272, as well as 297. I think Ms. Winchester may have that  
11 for you.

12 Doctor Montgomery, what information is contained in  
13 Defendant's Exhibit 267, 272 and 297?

14 THE COURT: You're not making inquiry about --

15 MR. CHARNES: 267 through 297.

16 THE WITNESS: 267, 268, 269, are graphs of NGH's  
17 stock price for two subject periods, and then for two  
18 subperiods, and then for the entire period from June 14,  
19 1999 through December 11, 2000.

20 270 is a graph of NA Stock price for June 14th  
21 through December 11th, then there are two subperiods  
22 following that, and then 297 is another subperiod for NGH's  
23 Stock price.

24 BY MR. CHARNES:

25 Q. Do all of the exhibits you just mentioned, is the

1 information you mentioned also contained in the graphs,  
2 price graphs in your expert report?

3 A. Yes. That's correct.

4 Q. And will Defendant's Exhibits 267 through 272 and DX  
5 297 assist your testimony today?

6 A. Yes, they will.

7 Q. Please turn to DX 288. What does Defendant's 268 show?

8 A. This is a graph of NGH's Stock price from June 14, 1999  
9 through January 31st, 2000. It shows that NGH declined  
10 fairly steadily through this entire period, with a  
11 particularly sharp decline on October 20th, 1999, when the  
12 Engle decision -- when the decision in the Engle case was  
13 announced.

14 Q. Would you please turn to Defendant's Exhibit 269. What  
15 does Defendant's 269 show?

16 A. 269 is a graph of NGH's Stock price from January 31st,  
17 2000, the time in which NGH and NA were first removed from  
18 the Plan, to December 11, 2000, when NGH was acquired by  
19 RJR. It shows that NGH's Stock price was relatively flat  
20 through February 2000, then began to rise in March 2000 and  
21 rose sharply after the announcement of Carl Icahn's bid on  
22 March 30th, 2000, and then after some dips in stock, rose  
23 substantially later in the spring of 2000.

24 Q. And finally on NGH, Doctor Montgomery, if you would  
25 turn to Defendant's Exhibit 227 and explain what that



1 exhibit shows.

2 A. Okay. This is a graph -- this is a graph that combines  
3 the information on Exhibits 268 and 269. It is a graph of  
4 NGH from the entire period from June 14, 1999 through  
5 December 11, 2000 and so, therefore, shows the decline of  
6 NGH in 1999 and then the increase in NGH 2000.

7 Q. Doctor Montgomery, did you hear testimony in this trial  
8 regarding a October 8, 1999 meeting regarding the Capital  
9 Investment Plan?

10 A. Yes, I did.

11 Q. Did you determine what the postspin performance of the  
12 NGH Stock would have looked liked as of October 8th, 1999?

13 A. Yes. I did. That information would be shown in  
14 Exhibit 297 and that is a graph of the return in NGH's Stock  
15 price from June 14, 1999 through October 8, 1999. I would  
16 like to add one small detail. The June 14th price for NGH  
17 is what is known as split adjusted. The actual stock price  
18 would have been a lot higher before the spin-off, but this  
19 is adjusted and adjusted for the spin-off. It's what the  
20 price would be if you took the spin-out out on June 14th.  
21 June 14th itself is something of a constructive, but this  
22 graph shows the actual prices from June 14. The spin-off  
23 adjusted stock price date is also dated -- it's typically  
24 used by investors.

25 Q. Doctor Montgomery, if you please turn to Defendant's

1 Exhibit 271.

2 THE COURT: When you reach a convenient stopping  
3 place, you let us know.

4 MR. CHARNES: Your Honor, I think we should do it  
5 now.

6 THE COURT: Okay. Anything we should talk about  
7 before we take our afternoon recess?

8 MR. LEWIS: No, Your Honor.

9 MR. CHARNES: No, Your Honor.

10 (Recess taken from 3:25 p.m. to 3:46 p.m.)

11 BY MR. CHARNES:

12 Q. Doctor Montgomery, if you please turn to Defendant's  
13 Exhibit 271.

14 A. Okay.

15 Q. And with respect to the NA Stock, what does DX 271  
16 show?

17 A. DX 271 shows NA's Stock price from June 14th, 1999  
18 through January 31st, 2000. And, it shows fairly steady  
19 decline in the stock throughout this period, obviously with  
20 some up's and down's.

21 Q. If you please turn to DX 272.

22 A. Okay.

23 Q. And what does DX 272 show?

24 A. It shows NA Stock price from January 31st, 2000 through  
25 December 11th, 2000. It shows that NA continued to trend

1 down from January 31st into March 2000, and then rose quite  
2 sharply after the Icahn bid on March 30, 2000, and rose  
3 throughout the spring of 2000, and then flattened out after  
4 the acquisition of NA by Phillip Morris was announced in  
5 June of 2000.

6 Q. If you turn to DX 270 and explain what that exhibit  
7 shows.

8 A. This shows NA Stock price for the combined periods of  
9 the previous two exhibits that we discussed, running from  
10 June 14th, 1999 through December 11, 2000.

11 Q. A few minutes before the break, did you testify that it  
12 was your opinion, that the stock price appreciation of NGH  
13 and NA, after March of 2000, was not the result of  
14 predictable factors in the marketplace?

15 A. Yes, I did testify.

16 Q. And what analysis did you perform in reaching that  
17 opinion?

18 A. Well, it follows from the general opinion that there is  
19 no reason to expect extraordinary returns based on public  
20 information, moreover, I reviewed analyst reports for any  
21 indication that these increases and chain of events that  
22 started with Carl Icahn's bid and ended with the acquisition  
23 of NA and NGH, was anticipated by analysts. I also reviewed  
24 news articles on Nabisco from June 14th, 1999 through March  
25 of 2000 and after March of 2000 as well, and found no

1 indication that the chain of events that ensued in  
2 March 2000 was anticipated.

3 Q. Doctor Montgomery, I would like you to please return to  
4 your expert report, which is DX 60, which is in notebook  
5 two.

6 MR. CHARNES: Your Honor, that's in notebook two,  
7 and in particular, Exhibit 18.

8 BY MR. CHARNES:

9 Q. Exhibit 18 to DX 60.

10 A. I've got it.

11 Q. What is Exhibit 18 to Defendant's Exhibit 60?

12 A. Exhibit 18 to Defendant's Exhibit 60 is a graph of  
13 three lines. The dark blue line is Nabisco -- was NA's  
14 Stock price from December 31st, 1998 through December 11,  
15 2000. The red line is an index, an equal weighted index of  
16 other companies in the packaged food industry. The name of  
17 companies are listed in the footnote to the exhibit, and the  
18 green line is the overall market, as shown by S&P 500 Index.  
19 What this shows is, that the price that -- the drop of NA  
20 Stock price throughout 1999 and early 2000, was similar to  
21 the drop in prices of other companies in the package food  
22 industry, and what this indicates is, that the decline in NA  
23 over this period was largely due to the declining value of  
24 food companies in the marketplace.

25 Q. And what, if anything, does Exhibit 18 indicate to you

1 with respect to the performance of NA Stock after  
2 January 31st, 2000?

3 A. Well, it indicates -- first of all, it's the same  
4 information that where in the exhibits of NA alone, and  
5 that's that NA continued to decline until late March 2000.  
6 Also, that decline was also in line with the continued  
7 decline of the other food stocks, so it was continuing  
8 disfavor in the market of the food stocks.

9 This, by the way, was during basically the tech boom,  
10 the NASDAQ boom and investors were very interested in stocks  
11 with high growth potential and food stocks were not seen as  
12 having high growth potential. Then on March 30, the Icahn  
13 bid was announced, and NA had a sharp increase. Other food  
14 stocks also began to increase around the same time, as  
15 several other mergers and acquisitions were initiated and  
16 announced in the food industry, including the acquisition of  
17 Best Foods by Unilever.

18 Q. Would you please turn to Exhibit 16. Using Exhibit 16  
19 to DX 60, please explain to the Court your opinions  
20 regarding the performance of NGH Stock during 1999.

21 A. Okay. This is a graph of the stock price of NGH from  
22 June 14, 1999 through December 11, 2000. It also shows the  
23 stock price for RJ Reynolds Tobacco, which is the red line,  
24 and it shows an index of other tobacco stocks, excluding RJ  
25 Reynolds, and that's the light blue line, and the stocks in

1 that index are listed in the footnote, and it also has for  
2 the previous graph, shows that the market, the S&P 500 Index  
3 in green.

4 What this shows is, that the decline of NGH from  
5 June 14, 1999 through early 2000, was in line with the  
6 decline of other -- well, of stocks in the tobacco industry,  
7 including RJ Reynolds, and also the stocks that are in the  
8 tobacco index, and the reason for this was, as I understand  
9 it, heightened concern over the risks for tobacco related  
10 companies of tobacco litigation and the sharp decline in  
11 late October was in reaction to the Florida Appeals Court  
12 decision in the Engle case on October 20th.

13 Q. Doctor Montgomery, with respect to the performance of  
14 NGH beginning in March of 2000, what opinion do you have  
15 based on Exhibit 16 to DX 60?

16 A. Well, the increase in NGH starting in late March was  
17 sharp, it was sudden. Other tobacco stocks improved  
18 somewhat during this period. RJ Reynolds improved, had a  
19 big increase. As I, you know, have said, the reasons for  
20 NGH's decline were related to, I think primarily concerns  
21 about tobacco related liabilities, as well as a decline in  
22 the underlying value of NA, which the other graph shows, and  
23 then the increase starting in March 2000 was related to the  
24 Icahn bid, and the fact that that unleashed the possibility  
25 of corporate restructuring that had previously been

1 considered basically off the table until mid 2001.

2 Q. Doctor Montgomery, did you testify earlier today, that  
3 you researched and reviewed available analyst reports and  
4 news articles regarding NGH and NA during the period of 1999  
5 to early 2000?

6 A. Could you repeat that question?

7 Q. Yes. Did you research and review analyst reports and  
8 news articles regarding NGH and NA from the time of the  
9 spin-off in June of 1999 through January 31st, 2000?

10 A. Yes, I did. And actually beyond January 1st, 2000 as  
11 well.

12 Q. In any of the materials that you read that were  
13 published before January 31st, 2000, did you see any  
14 indication whatsoever, that Carl Icahn might make an offer  
15 for NGH in the year 2000?

16 A. No. There was no mention of that possibility, or as  
17 best I can recall, of anybody else making an offer for  
18 either NGH or NA.

19 Q. If you please refer to Plaintiff's Exhibit 346, which I  
20 will get for you.

21 MR. CHARNES: I think it is in 12, Your Honor.

22 BY MR. CHARNES:

23 Q. Doctor Montgomery, what is Plaintiff's Exhibit 346?

24 A. This is a copy of an article in the Wall Street Journal  
25 for Friday, November 26, 1999, which is, by the way, the day

1 after Thanksgiving, or was the day after Thanksgiving, and  
2 it's a series of brief news items related to deals and deal  
3 makers. I guess the third item in here is a report of Carl  
4 Icahn's -- the fact that Carl Icahn had taken -- well, I'm  
5 sorry. The fact that Carl Icahn had purchased 6 million  
6 shares in Nabisco Group Holdings. So this is a report of  
7 the fact that Carl Icahn had acquired 6 million NGH shares.

8 Q. Do you know in fact whether that news article  
9 accurately reports Mr. Icahn's acquisition?

10 A. I don't have any additional knowledge other than the  
11 article on that subject.

12 Q. And what, if anything, did you do to analyze the impact  
13 of this newspaper article on the market for NGH Stock?

14 A. Well, I reviewed the stock prices of NGH and NA and I  
15 guess really for this article NGH would be more relevant.  
16 The return on NGH Stock price for November 26th. I found  
17 that there was no change in the price on November 26th,  
18 relative to the previous price, which would have been on  
19 Wednesday, the day before Thanksgiving. So there was no  
20 price reaction to this news regarding NGH. That's also true  
21 when we look at adjusted for the market.

22 Q. After November 26th, 1999, the date of that article,  
23 was there any indication in any source, whether an analyst  
24 report or an article in the media, mentioning the  
25 possibility of an offer for NGH by Carl Icahn?



1 A. No, there was not.

2 Q. Doctor Montgomery, in your opinion, is there certain  
3 information that is released public that is value relevant  
4 to potential buyers of a security that is not value relevant  
5 to potential sellers of the same security?

6 A. There is no information.

7 MR. LEWIS: Objection, Your Honor, new opinion.

8 THE COURT: Doctor Montgomery, would you.

9 (The witness left the courtroom.)

10 MR. LEWIS: It is possible I have forgotten  
11 something in one of his reports, but this is not leaping to  
12 mind as something I have heard any testimony about.

13 THE COURT: Okay.

14 MR. CHARNES: Your Honor, Doctor Biller testified  
15 on cross-examination specifically with respect to a New York  
16 Times article in March of 1999, that he believed the  
17 information in that article was relevant, was value relevant  
18 to potential buyers of RJR Nabisco Stock, but he did not  
19 opine that it was not relevant to people like the Plan that  
20 already held RJR Nabisco Stock, and testimony from Doctor  
21 Montgomery would be in direct rebuttal to Doctor Biller's  
22 testimony on the witness stands.

23 THE COURT: Was this an opinion that he had stated  
24 in either his original opinion or supplemental?

25 MR. CHARNES: It was not an opinion in either of

1 his reports. It was simply rebuttal to something Doctor  
2 Biller stated on the witness stand. More importantly,  
3 Doctor Montgomery believes it is not economically valid.

4 THE COURT: Mr. Lewis.

5 MR. LEWIS: I have nothing further to add, Your  
6 Honor.

7 THE COURT: What would allow that just as  
8 rebuttal? I said what would allow that just as rebuttal?

9 MR. CHARNES: I think that Doctor Biller testified  
10 to that on the stand, and I think it would be helpful  
11 information for the Court, and as a matter of fairness for  
12 Doctor Montgomery to -- that was an opinion that was not in  
13 Doctor Biller's reports, came out on cross-examination, for  
14 completeness for the Court, for Your Honor to hear Doctor  
15 Montgomery's view about whether that is an economically  
16 valid opinion or not.

17 To the extent that the Court might be considering  
18 ultimately relying on Doctor Biller's opinion on that, I  
19 guess our view is, that we would like the Court to hear, you  
20 know, a contrary economic view. If the Court believes it is  
21 irrelevant information, then obviously --

22 THE COURT: But that came out through your  
23 examination?

24 MR. CHARNES: It came out through my examination  
25 of Doctor Biller, correct.

1           THE COURT: I'll sustain the objection.

2 BY MR. CHARNES:

3 Q. Doctor Montgomery, I would like to turn your attention  
4 to the subject of damages in this case.

5 A. Okay.

6 Q. Did you in fact calculate, assuming that the Court  
7 finds liability on behalf of the Plaintiffs here against  
8 Defendants, did you in fact calculate damages that the class  
9 would be entitled to?

10 A. Yes, I did.

11 Q. And over what periods of time did you calculate the  
12 damages?

13 A. I calculated damages from June 14th, 1999 up through  
14 December 11, 2000, and then I additionally calculated the  
15 damages adding several different returns to those damages  
16 and calculated damages through September 30th, 2009.

17 Q. And what data did you use in order to make full sets of  
18 calculations, that is calculations of losses up to  
19 December 11, 2000, and then from December 11, 2000 through  
20 the end of September 2009?

21 A. The primary data that I used to do the calculation of  
22 the losses up through December 11, 2000, was a data set that  
23 was provided that contained three files of data from the  
24 Plan's record keeper, that is a data set of all transactions  
25 by the participants who held NGH or NA on June 15th, 1999.

1 Also, there was another data file that contained the  
2 quarterly balances in each fund for each participant, and  
3 that information was also broken up by each subaccount in  
4 each participant's -- in each participant's account and  
5 subaccounts or for different sources of money, such as after  
6 tax and before tax contributions.

7 The final file was a daily file of unit values for each  
8 investment option in the Plan, and these data originally  
9 covered the period, as I mentioned earlier in my testimony,  
10 from the middle of 1997 through the end of 2002. The part  
11 that was relevant for my calculations, was from June 1999  
12 through December of 2000.

13 Q. And, Doctor Montgomery, you mentioned that the third  
14 included daily fund unit values. Is it correct that it  
15 included unit values rather than share prices because these  
16 were unitized funds in the Plan?

17 A. That's correct. And that's with respect to the three  
18 single stock funds; NGH, NA and RJ Reynolds Tobacco.

19 MR. CHARNES: I would just like to note for the  
20 record in evidence are two compact disks, DX 159 and DX 161.  
21 These contain participant data that Doctor Montgomery just  
22 testified to and have been relied on to calculate potential  
23 damages. The parties executed a stipulation dated  
24 April 4th, 2008, that has been heard previously in this  
25 trial, that is PX 295, and pursuant to that stipulation, the

1 data on these compact disks are true and accurate Plan  
2 participant data, and the parties also stipulated that they  
3 are business records under Rules of Evidence 803.6, and that  
4 they meet the authentication requirement of Federal Rules of  
5 Evidence 901.A.

6 We have not yet formally filed that with the  
7 electronic ECF, but we will do so. I just wanted to alert  
8 the Court that is the data on which Doctor Montgomery is  
9 going to be testifying.

10 THE COURT: Okay.

11 BY MR. CHARNES:

12 Q. Doctor Montgomery, I would first like to turn your  
13 attention to the appreciation damages and that is the  
14 damages that existed up through December 11, 2000. What  
15 methodology or methodologies did you use in order to  
16 calculate those damages?

17 A. These damages were calculated -- the basic approach is  
18 to look at the difference in money that participants would  
19 have had as of December 11, 2000, if they had retained their  
20 NGH and NA investments up until that point. The difference  
21 between what they would have had and what they actually had,  
22 and in order to calculate that difference, you need to  
23 analyze which of the investments that they actually made  
24 that would not have made had they retained their NGH and NA  
25 holdings, so that calculation boils down to an analysis of

1 the difference between the proceeds of investing in NGH and  
2 NA, and the proceeds of the alternative investment that they  
3 would not have made had they retained their NGH and NA  
4 holdings, and the investment that they would not have made  
5 is one of the investments that they actually made.

6 Q. And what methods did you use in order to calculate  
7 damages along those lines?

8 A. Well, there are two approaches to determining which  
9 investments -- investment or investments each participant  
10 would not have made had they retained their NGH and NA  
11 investments. The first approach is tracing, that is to  
12 follow the money that the participants took out of NGH and  
13 NA, either voluntarily before January 31st, or as part of  
14 the liquidation on January 31st, and follow that into  
15 whatever fund it was transferred into, and then continue to  
16 follow that money, and if it was subsequently moved to any  
17 other investment fund, and also, consider if the money was  
18 in fact withdrawn from the Plan, that would be part of the  
19 calculation as well. But all of that is the tracing of the  
20 methodology that follows where the money taken literally  
21 went, if you will.

22 The other approach that I took is, I refer to the most  
23 similar approach, and that takes the approach that instead  
24 of looking at the Nabisco money, the money coming out of the  
25 Nabisco Funds in isolation, it is more appropriate to keep

1 in mind that a participant is likely to be looking at his or  
2 her entire portfolio within the Plan as a portfolio, and  
3 would be interested in the mix of investments that he or she  
4 has, and so if that participant isn't permitted to retain  
5 his or her investment in NGH or NA, he or she would likely  
6 invest that money in the investment that's the most similar  
7 to NGH and NA, and that would be an effort to have an  
8 investment portfolio as close to being the portfolio they  
9 would have with NGH and NA, in lieu of having NGH and NA.  
10 That approach is what I referred to as the most similar  
11 analysis. It takes as a premise that the Plaintiff's are  
12 managing their investments as a portfolio.

13 Q. What alternative investments in the Plan did you  
14 determine were most similar to NGH and NA?

15 A. I performed an analysis of all the different investment  
16 options in the Plan, and looked at their degree of  
17 similarity to NGH, NA on two dimensions. One of those  
18 dimensions was the degree of volatility of those  
19 investments, remembering that volatility is the variability  
20 of daily returns, and I ranked separate for NGH and NA, I  
21 ranked the other investment options according to how similar  
22 they were; how close the volatility was to NGH.

23 Some of the details of this in my original expert  
24 report. The other dimension I considered in assessing the  
25 similarity was the area of correlation of the other

1 investment options with NGH or NA. The more correlated an  
2 investment option is with NGH or NA, the more similar it is.  
3 I used these two methods because risk as well as return are,  
4 in my opinion, the relevant considerations for making  
5 investments, so looking at the different aspects of risk is  
6 the appropriate way to measure the similarity of investments  
7 with NGH or NA.

8 When I did this, I determined that the most similar  
9 investment to NGH was in fact RJ Reynolds Tobacco. It, like  
10 RJ Reynolds Tobacco, NGH has high volatility. In addition,  
11 NGH and RJ Reynolds are highly correlated with each other,  
12 so RJ Reynolds Tobacco is the most similar investment to  
13 NGH.

14 The most similar investment to NA, I determined to be  
15 the -- I'm actually forgetting. I think it's the Total  
16 Stock Fund. It is one of the diversified stock funds. I  
17 can refresh my memory on that.

18 Q. Yes. Please turn to your report, if that will be  
19 helpful.

20 A. Exhibit 30 of my original report shows the details of  
21 this analysis. The most similar fund for NA was in fact the  
22 Total Stock Market Fund, which was an index investment in  
23 the entire U.S. Stock Market.

24 Q. Doctor Montgomery, as between the tracing method and  
25 the most similar investment method that you've just



1 described, do you have an opinion as to which you believe is  
2 the most accurate method for computing damages in this case?

3 A. My opinion is, that the most similar method is more  
4 accurate, it takes into account what -- instead of looking  
5 at simply tracing Nabisco money in isolation, it takes into  
6 account the whole of what a participant looking at a  
7 portfolio of investments would do, and comes up -- tries to  
8 come up with what would be what that participant managing  
9 the risk would likely to do if that participant didn't have  
10 available NGH or NA.

11 MR. LEWIS: Motion to strike, Your Honor.

12 THE COURT: Would you.

13 THE WITNESS: Step out?

14 THE COURT: Please.

15 *(The witness left the courtroom.)*

16 MR. LEWIS: It's him giving an opinion about what  
17 participants would do, which I believe is outside the scope  
18 of his expertise. There are other problems we have with  
19 this also, if we get to those.

20 MR. CHARNES: Your Honor, it's based on his  
21 background and expertise. It's his opinion about how  
22 investors behaved. Again, he testified that he believes  
23 based on his training and experience in economics, he has  
24 the expertise to describe how investors overall behaved. He  
25 said he was not an expert in how person A or person B

1 behaves, but that economists are competent to testify about  
2 how investors as a group behave in the stock market, that  
3 would translate --

4 THE COURT: Investors in a plan, in this Plan?

5 MR. CHARNES: Overall based on his -- I think he  
6 testified to that during voir dire, but I think that his  
7 opinion is based on his expertise in how investors behave.

8 THE COURT: I'm going to let you ask him those  
9 questions, and tell you that you have a very high bar to go  
10 over to get this in, but I'll let you ask him those -- how  
11 he arrives at his decision of how those investors would  
12 behave, especially when it's been his earlier testimony,  
13 that a huge percentage of people in that Plan never moved  
14 anything.

15 MR. CHARNES: Your Honor, I think he already did  
16 testify about his -- how he arrived at the -- what you call  
17 the most similar and best method, and how he assumed -- how  
18 he calculated where that money would go but for the removal  
19 of the funds. That is a --

20 THE COURT: If that's the basis of it, the  
21 objection is sustained. If you have an additional basis for  
22 it, I'll hear it.

23 MR. CHARNES: Thank you. I'll just move on, Your  
24 Honor.

25

1 BY MR. CHARNES:

2 Q. Doctor Montgomery, it's true, is it not, that the NGH  
3 and NA Funds did not exist in the Plan after January 31st  
4 are 2000?

5 A. Yes, that is true.

6 Q. How did you calculate what those two funds would have  
7 earned if they had remained in the Plan after January 31st,  
8 2000 up until December 11th, 2000?

9 A. Well, in order to do that calculation, I considered  
10 several different methods. The one method that I considered  
11 was statistical analysis of the relationship between daily  
12 returns of the NA and NGH Stock Funds from this analysis  
13 separately for both stock funds.

14 The statistical analysis of the relationship of the  
15 return of those stock funds, the daily returns on the  
16 June 14th through December -- I'm sorry, through  
17 January 31st, 2000 period, to the daily returns of the  
18 underlying stocks of the NGH and NA Stock, and that  
19 statistical analysis -- the statistical analysis I used was  
20 the regression analysis, the relationship of daily returns.  
21 I also considered looking at using the information on the  
22 cash levels in both the NGH and NA Stock Funds, and as you  
23 presumably know, each stock fund contains mostly the  
24 underlying stock, but also contains some cash, some other  
25 underlying short term investments.

1           One of the other ways to do it is, to look at the  
2     percentage of cash, percentage of short term investment and  
3     then project the returns, assuming that the stock had -- the  
4     stock portion of the stock fund had the underlying stock  
5     return, the cash had a zero percent return and the short  
6     term investments maybe had a small interest return. That's  
7     the other possible way to project the NGH and NA returns  
8     after January 31st. So I did this, looked at these both  
9     ways.

10           In order to assess which of those was better, I  
11     performed the exercise for the one single stock fund that I  
12     did have data from throughout this period, from June 14,  
13     through December 11, 2000; that's the RJ Reynolds Common  
14     Stock Fund. I did the same exercise for the RJ Reynolds  
15     Stock Fund in the data up through -- doing the regression up  
16     through January 31st, 2000, and also doing the projection  
17     based on the cash levels in that stock fund as of  
18     December 31st, 1999. I found that the regression approach  
19     predicted much more closely the actual return in the RJ  
20     Reynolds Common Stock Fund over the period from  
21     January 31st, 2000 to December 11, 2000, and using the cash  
22     levels on December 31st, 2000. So, that is why I decided to  
23     use the regression approach for projecting the NGH and NA  
24     Common Stock Funds and fund returns from the hypothetical  
25     Common Stock Fund returns from January 31st, 2000 through

1 December 11, 2000.

2 Q. Doctor Montgomery, were you required to make -- in  
3 addition to what you already testified to, were you required  
4 to make other assumptions in your analysis using the tracing  
5 method or most similar fund method of calculating damages?

6 A. Yes, I was.

7 Q. Would you please generally describe what those  
8 assumptions were and why you think that they were valid.

9 A. Okay. The list of assumptions is -- it's all in the  
10 expert report, and I think I might be -- if I could, I could  
11 just use the expert report to refer to. It is probably the  
12 easiest way to answer this question. And this is  
13 Defendant's Exhibit, what is it --

14 THE COURT: 60.

15 MR. CHARNES: It should be Defendant's Exhibit 60.

16 THE WITNESS: Right. The list of assumptions that  
17 needed to be made for the tracing method are listed in  
18 Exhibit 60 in Paragraph 81 on Page 27 of my report. One of  
19 the assumptions is, that money in a particular source  
20 account such as the before tax employee contribution, stayed  
21 in that account, and this -- we confirmed this assumption by  
22 analyzing all of the Plan data that we received, and we  
23 confirmed that money that was in one account never got  
24 transferred to another account -- money -- it stays in the  
25 particular source account that it starts in.

1           The other assumptions are listed that are all for  
2 the basis of identifying where money that goes out of a  
3 particular investment option, identifying when the money  
4 that goes out is money that had begun its journey as NA or  
5 NGH money. Those are all here. I'm not sure if I should go  
6 through that detail.

7           There are also, I believe, some assumptions on the  
8 most similar method. Let's see if I can find --

9           THE COURT: I don't know that you need to do that  
10 for the most similar method.

11 BY MR. CHARNES:

12 Q. Doctor Montgomery, without discussing the assumption in  
13 particular, if you could just talk generally -- describe  
14 generally for the Court how you tested -- whether you tested  
15 the assumptions to assure that they were accurate and not  
16 bias in your result one way or the other.

17 A. Yes, I did. Whenever there was an assumption that  
18 there seemed to be more than one conceivable way to approach  
19 it, I calculated damages both ways, and satisfied myself --  
20 first of all, I chose the approach that I felt was the most  
21 reasonable, but I also satisfied myself that where there was  
22 a reasonable argument about the assumption, that the  
23 alternative would not make any significant amount of  
24 difference. For example, in the tracing method, I made the  
25 assumption last in, first out, which is the last money put

1 into an investment is the first money taken out. I also  
2 estimated damages on using the opposite assumption, which is  
3 FIFO, which is first in, first out, which is the first money  
4 into an investment is the first money that's taken out. The  
5 overall aggregate damages were something like one percent  
6 higher using FIFO, so it's not a very significant  
7 difference.

8 Q. Doctor Montgomery, do you have an opinion as to whether  
9 your damages methodology is preferable to the methodology  
10 used by Mr. Altman in calculating the damages?

11 A. Yes, I do.

12 Q. What is that?

13 A. I believe it is preferable.

14 Q. Have you determined whether Mr. Altman's damages  
15 calculations considered the actual returns received by  
16 participants when they liquidated Nabisco Holdings?

17 A. Yes. I have determined that he did not do that. He  
18 assumed that all participants got the average return  
19 realized by the entire Plan, not even just by the portion of  
20 the Plan made up by the participants who had held NGH and  
21 NA, whereas my analysis looked at the actual returns  
22 realized by each participant separately.

23 Q. Did any of the participants receive the returns that  
24 Mr. Altman used in his damages calculation?

25 A. I don't think I actually know that. It would be highly

1 unlikely that any participant got the average Plan return,  
2 no.

3 Q. Do you have an opinion as to whether Mr. Altman's use  
4 of the actual NGH and NA stock prices to estimate returns up  
5 through December 11, 2000, was appropriate?

6 A. Yes. I do have an opinion. In general, using the  
7 actual NA and NGH Stock prices through December 11, 2000,  
8 overestimates the returns that participants would have  
9 received from investments in the NA and NGH Stock funds,  
10 because according to my analysis, as well as general  
11 experience, single stock funds that contain cash and incur  
12 transaction costs, expenses and fees, typically underperform  
13 the actual underlying stocks by some margin.

14 Q. Do you have an opinion as to whether Mr. Altman is  
15 correct that you overestimated the amount of cash held by  
16 the NGH Stock Fund?

17 A. I don't think there is any basis for Mr. Altman to say  
18 that one way or another. Mr. Altman, based that assertion  
19 on cash levels on one single day, December 31st, 2000, and  
20 the whole point of having a cash level was to provide a  
21 buffer for transactions, and cash levels are not constant  
22 and the December 31st cash level is not necessarily a good  
23 predictor of cash level on any other day.

24 Q. And you said December 31st, 2000?

25 A. Yes. I'm sorry, I did. And that was a misspeak. It



1 is December 31st, 1999.

2 Q. Have you determined how Mr. Altman addresses money  
3 withdrawn from the Plan by participants between June 14,  
4 1999 and the end of September, 2009?

5 A. The end of September 2009?

6 Q. Yes. From June 14, 1999, up to the end of his damages  
7 calculations.

8 A. Yes. Mr. Altman assumes that no participant, no class  
9 members withdrew any money from the Plan during this time.  
10 His damages are based on the assumption that all money  
11 stayed in the Plan. What I did, on the other hand, through  
12 December 11, 2000, was assume that where participants had  
13 taken out some of the investment that they made instead of  
14 NA or NGH, they would have also taken out money if they kept  
15 their money in NGH or NA.

16 Q. Do you believe that Mr. Altman's assumption that no  
17 money was withdrawn from the Plan is a valid assumption?

18 A. No. I think It's clearly unrealistic. There are all  
19 sorts of reasons that people would remove money from the  
20 Plan, and it makes no sense to me to believe that if they  
21 had retained NGH or NA, they would not have made any  
22 withdrawals.

23 Q. Have you determined whether Mr. Altman correctly  
24 considered the timing of sales of NGH and NA Stock by the  
25 trustee.

1 A. Well, Mr. Altman's analysis is based on the  
2 transactions by the trustee, the sales by the trustee of NGH  
3 and NA. Those sales were not necessarily and generally not  
4 done on the same date that participants transferred their  
5 money out of NA and NGH, and this is obviously the case with  
6 the participants who were forced out of the Plan, out of NGH  
7 and NA on January 31st, 19 -- January 31st, 2000. The  
8 persons who were forced out on that day received the closing  
9 value of the NA and NGH Stock Funds on that day, which was  
10 based on the closing price of NA and NGH. The sales by the  
11 trustee were not until early February, so they were at  
12 different prices. Any gains or losses would have been  
13 incurred by the Plan overall, and not by the individual  
14 participants.

15 Q. Going back to the withdrawal of money from the Plan, I  
16 just have one further question, which is based on your  
17 analysis of data, did participants actually in fact withdraw  
18 money from the Plan during the periods in question?

19 A. Yes, they did. Well, my analysis confirmed that they  
20 did up through December 11, 2000. I didn't do any specific  
21 analysis of the period after December 11, 2000.

22 Q. Do you have an opinion as to whether Mr. Altman  
23 correctly calculated the Plan's returns during the year --  
24 calendar year 2008 and the first three quarters of 2009?

25 A. I do have an opinion. Mr. Altman greatly overstated

1 the Plan's returns in 2008. He made a basic mistake with  
2 calculating the weighted average of Plan returns for 2008.  
3 He used the balances in each investment fund as of the end  
4 of the year, rather than at the beginning of the year, and  
5 if he used the weights as of the end of the year, you are  
6 going to greatly underweight any investment that did poorly  
7 during that year and overweight any investment that did  
8 well.

9 As we all know, 2008 was a terrible year for stocks,  
10 and so if you used end of period rates, you are going to  
11 greatly underrate the return on stocks during -- the stock  
12 funds during 2008 and, therefore, greatly understate the  
13 overall negative return of the Plan. So on that basis  
14 alone, Mr. Altman greatly understated the loss that the Plan  
15 incurred in 2008 due to poor stock market.

16 In addition, Mr. Altman used form 5500 data to  
17 calculate his Plan returns for every year up through 2007,  
18 and in his initial report, clearly showed a view that form  
19 5500 data was the better way to calculate returns than using  
20 investment returns. Form 5500 data was available, at least  
21 has been available recently for calendar year 2008, and it  
22 is -- was initially provided in the form 11-K filing for  
23 2008 in a note of that filing, and if you use that, the data  
24 in the note to the 11K that's the form 5500 data, you get a  
25 negative return for the Plan for 2008, that's fairly close

1 to the return you would get if you do a proper weighted  
2 average based on beginning of the year balances.

3 At any rate, Professor Altman -- I'm sorry, Mr. Altman,  
4 greatly overstated the Plan's return in 2008.

5 He made a similar mistake with weights in 2009, in that  
6 he appears to have used the end of the third quarter weights  
7 to calculate his average returns for 2009, whereas I believe  
8 the more proper thing to do would be to use the beginning of  
9 period weight for 2009, and if -- I did that and I get a  
10 negative -- a positive return for 2009. It is somewhat less  
11 than the positive return Mr. Altman used for 2009. So if  
12 you add those together, the overall return that Mr. Altman  
13 had for the Plan for 2008 or 2009 was substantially  
14 overstated.

15 Q. Did Mr. Altman's overstating of the returns in 2008 and  
16 2009, have the effect of overstating damages or understating  
17 damages?

18 A. It had the effect of overstating damages when the Plan  
19 return was used for the calculation.

20 Q. Did Mr. Altman's damages methodology allow him to  
21 calculate damages, if the Court decides ultimately to  
22 exclude early sellers or participants who signed releases?

23 A. No, it does not. There is no information in  
24 Mr. Altman's calculation about any damages for individual  
25 participants and so you can't exclude portions of the class.

1 Q. Doctor Montgomery, to go back briefly to your opinion  
2 with respect to Mr. Altman's calculation of Plan returns in  
3 2008 and 2009, is your reason for criticizing Mr. Altman's  
4 calculation of Plan returns for the first three quarters of  
5 2009, in other words, his using the end of quarter returns  
6 instead of the beginning of the quarter returns the same  
7 reason that you articulated for the calendar year 2008?

8 A. Yes. It's essentially the same. Well, the mistake  
9 Mr. Altman did is the same. I think in addition, one can  
10 calculate the 2008 return using the same methodology that  
11 Mr. Altman had used in previous years, but you got a  
12 relatively fairly similar return to the return you would use  
13 if you corrected Mr. Altman's mistake for 2008, which is the  
14 same mistake he made for 2009.

15 Q. Do you have an opinion as to whether Mr. Altman was  
16 correct in that the participant level data on which you  
17 relied for your damages, were not accurate?

18 A. I believe that opinion of Mr. Altman is incorrect. My  
19 staff reviewed that data closely. They verified that the  
20 data was consistent. All of the balances agreed with all  
21 the transactions, sort of the way you balance a checkbook,  
22 you add up all the positive entries, you subtract the  
23 negative entries and you get your balance and everything  
24 works out, so my opinion is, that the data are reliable.

25 Q. And do you have an opinion with respect to Mr. Altman's

1 criticism of your approach, that your methodology did not  
2 reflect what actually happened in the Plan, beginning with  
3 the liquidation of the Nabisco Fund?

4 A. Yes. I believe that that is based on a  
5 misunderstanding of the Plan data by Mr. Altman. He took --  
6 that opinion, I think, was largely based on a table that was  
7 in some working papers that NERA had produced in response to  
8 a subpoena that combined data for the lead Plaintiff,  
9 Mr. Tatum, and combined the data for all of the different  
10 source of accounts into one overall account, and I also  
11 believe that Mr. Altman's commentary about that data doesn't  
12 really make sense if you read it closely, but if you do, if  
13 you look carefully at the data, subaccount by subaccount,  
14 you can see that the approach I took makes sense, and I  
15 believe is the correct approach.

16 Q. Doctor Montgomery, do you have an opinion about whether  
17 Mr. Altman is correct in his own opinion that you  
18 understated Mr. Tatum's personal damages by about \$10,000?

19 A. I believe that is incorrect. I believe that the review  
20 of the numbers that we have calculated, and I believe they  
21 are correct -- again, this is based on a combination,  
22 combining data from different subaccounts, which I believe  
23 is an inappropriate thing to do for tracing.

24 Q. I would like you to turn to PX 296, which Mr. Altman's  
25 report.

1           MR. CHARNES: That's in plaintiff's binder 11,  
2 Your Honor.

3 BY MR. CHARNES:

4 Q. Doctor Montgomery, I would like you to read for the  
5 record the paragraph at the top of -- excuse me, if you  
6 refer to Page 5 of Mr. Altman's report. For the record,  
7 this is his rebuttal report, Your Honor, Plaintiff's Exhibit  
8 296.

9 Are you there, Doctor Montgomery?

10 A. Yes.

11 Q. Would you please read the paragraph at the top of Page  
12 5.

13 A. "Mr. Montgomery's methodology does not reflect what  
14 actually happened. His calculation assumed investments made  
15 in RJR Stock on February 2nd remained in RJR Stock until a  
16 later sale or transaction, but it does not consider other  
17 transactions occurring on February 2nd. By examining  
18 document Montgomery 2212, Exhibit A, one can see that  
19 Mr. Tatum did not invest \$7,912 in the RJR Stock Fund on  
20 February 2nd, 2000. According to the data on that same day,  
21 \$6,407 was transferred from the RJR Stock Fund into the  
22 Vanguard Funds. The actual investment in Vanguard Funds on  
23 that date totaled \$28,877 times two funds or \$57,754. See  
24 Exhibit A. And the amount remaining in the RJR Stock Fund  
25 was \$7,912, less \$6,407, or \$1,505. Since Mr. Tatum held

1 much less RJR Stock than Mr. Montgomery assumed, the ending  
2 value of his actual investment was lower, and Mr. Tatum's  
3 damages was 131,444, not 121,204. See Exhibit B. The  
4 corrected damages amount is \$10,240 greater than  
5 Mr. Montgomery's model calculated.

6 "Defendant's methodology assumed that there were no  
7 other transactions occurring on the same day Mr. Tatum  
8 purchased RJR shares, which produced results that are  
9 inaccurate and understate damages. This example calls into  
10 question the reliability of Mr. Montgomery's calculations,  
11 even assuming his methodology is generally credible. See  
12 above."

13 Q. Now, with reference to Exhibit 18 to your report,  
14 actually the corrections to your report, which is DX 65,  
15 Exhibit 18 to DX 65, would you please explain whether you  
16 have an opinion as to whether Mr. Altman's criticism was  
17 correct or not.

18 A. Yes. This exhibit shows the details for the four  
19 subaccounts in Mr. Tatum's Plan account, and it shows the  
20 activity in each of those four subaccounts. I believe it is  
21 inappropriate to combine those subaccounts, and so that I  
22 believe my methodology using these four subaccounts is the  
23 proper approach.

24 Just as an example of why subaccounts are important,  
25 the second subaccount is the basic after tax money. It is



1 important, I think obviously, to segregate the money that  
2 exists in the Plan in an after tax basis, and you would not  
3 want to combine that and comingle that with before tax  
4 money, and so that's one of the purposes of these  
5 subaccounts is, to keep before tax and after tax money  
6 separate.

7 I can walk you through these if that would be  
8 appropriate.

9 Q. Yes. If you could briefly do so, that would be  
10 helpful.

11 THE COURT: Would you like to give me a chance to  
12 get this?

13 MR. CHARNES: DX 65.

14 THE COURT: I've got it. But I missed about a  
15 page of his testimony while I was looking for it.

16 THE WITNESS: My apologies.

17 THE COURT: Doctor Montgomery, if you could go  
18 back and explain again, using -- the part about the  
19 subfolder.

20 BY MR. CHARNES:

21 Q. Explain why it is important -- whether it is important  
22 to keep the different subaccounts separate in the damages  
23 calculation.

24 A. Yes. The reason is, that for tax purposes, and  
25 potentially other purposes, money that is identified as one

1 particular source, needs to be kept distinct from other  
2 sources in a 401(K) plan. If you look at the first page of  
3 my corrected Exhibit 18, you will see that two of the  
4 subaccounts -- these are headings all the way over on the  
5 left-hand side of the page, two of the subaccounts are the  
6 basic pretax and basic after tax. After tax contributions  
7 are contributions in which participants have already paid  
8 income taxes, which before tax contributions are  
9 contributions in which they have not yet paid taxes, and it  
10 is obviously important to keep those two sources separate  
11 from each other in the Plan accounts, and then there are two  
12 other subaccounts which are shown on the next page that the  
13 ESOP match and the company cash match, and all four of these  
14 accounts are separated in the Plan account data that we  
15 received.

16 Q. With reference to corrected Exhibit 18 in DX 65, can  
17 you use this exhibit to explain why Mr. Altman's criticisms  
18 of your damages methodology are not correct in your view?

19 A. Yeah. Just referring first to what Mr. Altman stated  
20 in his rebuttal report, he appears to be claiming that only  
21 \$1,505 of the money taken out of the NGH Fund by Mr. Tatum  
22 ended up in the RJ Reynolds Common Stock Fund, and so let me  
23 explain why I come up with a different number, and this  
24 requires that you walk-through all four subaccounts.

25 THE COURT: Let me get back there again.

1 THE WITNESS: It is again Exhibit 18, corrected  
2 Exhibit 18.

3 THE COURT: You hold right where you are.

4 THE WITNESS: DX 65.

5 THE COURT: You are on Page 1 or Page 2 of that?

6 THE WITNESS: I'm on Page 1, Your Honor. I'm just  
7 going to walk-through this sort of line-by-line.

8 Let's start with the first subaccount, which is  
9 the basic pretax. The second line of numbers there shows  
10 the balance that Mr. Tatum had in this subaccount, the basic  
11 pretax account on January 31st, 2000, and you can see that  
12 in the NGH Common Stock column, he had a balance of \$12,863.  
13 Now, that balance of 12,863, got forced out of NGH the next  
14 day on February 1st, and all of the money that was forced  
15 out of NGH and NA, got transferred into the Interest Income  
16 Fund, so the first line -- the next line shows the negative  
17 entry in the NGH account equal to the balance on  
18 January 31st, and then there is a positive entry the next  
19 line down, where it says 2/1/2000 fund transfer, and in  
20 there, there is a positive \$12,863 entry for the Interest  
21 Income Account.

22 So as of February 1st, that NGH money that was in  
23 the subaccount ended up in the Interest Income Fund. The  
24 next day, February 2nd, you see a negative entry for \$12,868  
25 under Interest Income Fund, and the reason it's not exactly

1 the same as the day before is, that there were actually two  
2 days of interest. There is interest from January 31st to  
3 February 2nd on that money, so it's going to be a little bit  
4 more, and you can -- so any way, the money was transferred  
5 out of the Interest Income Fund, and the next line shows  
6 where the money was transferred into; February 2nd, 2000,  
7 fund transfer in. You've got 870 going into the RJRT Common  
8 Stock Fund, 5,999 into each of the Vanguard Total  
9 International Fund, and the Vanguard Total Stock Fund. So,  
10 based on this account, the subaccount, the NGH money went a  
11 little bit into the RJRT Fund and mostly into the two  
12 Vanguard funds, so that's one subaccount.

13 Now the next subaccount, one has to look at --  
14 basically perform the same exercise. If you go back to the  
15 basic after tax, which is the bottom part of the first page  
16 of Exhibit 18, and read across on the January 31st, 2000  
17 line, you can see that in this subaccount the basic after  
18 tax account, this was \$19,819 worth of investment in NGH  
19 Fund, January 31st, 2000. That money got transferred out  
20 the next day, forced out, and transferred into the Interest  
21 Income Fund, and you can see a positive entry of \$19,819 in  
22 the Interest Income Fund. The next day, that money got  
23 transferred out of the Interest Income Fund or, again,  
24 reflecting two days worth of interest, and that \$19,826 got  
25 spread into the same three funds as the previous subaccount;

1 the RJRT Common Stock Fund, the Vanguard Total International  
2 Fund and the Vanguard Total Stock Fund; however, the amount  
3 going into the RJRT Fund was greater, was \$3,278.

4           Onto the next page. The next page shows the ESOP  
5 match subaccount, and if you look at the data for the  
6 balance in the ESOP match in January 31st of 2000 and read  
7 across to NGH Common Stock line, there is actually a box  
8 around this line, there is no balance.

9           In this subaccount, Mr. Tatum had no investment in  
10 the NGH account, so we would not need to look at this  
11 account to trace Mr. Tatum's NGH money and see where it  
12 went. You can see -- by the way, if you look at the RJRT  
13 Common Stock Fund under this subaccount that there was  
14 actually a transfer out in the ESOP fund of \$6,407. It was  
15 a transfer out of the RJRT Fund, but the important thing is,  
16 that that transfer out was not money that can be traced to  
17 the NGH Common Stock Fund, because this subaccount had no  
18 investment in the NGH Common Stock Fund, and this is the  
19 mistake Mr. Altman makes is, he's mixing these sources up,  
20 when they actually are distinct.

21           Then the final subaccount is the company match  
22 fund. This is the bottom of the second page. In the  
23 company match fund, Mr. Tatum had a balance on January 31st,  
24 2000 of \$26,554 in the NGH Common Stock Fund. That money  
25 got forced out into the Interest Income Fund, and so you

1 have a transfer in of that same \$26,554 on February 1st,  
2 2000, into the Interest Income Fund, and the next day, that  
3 money, plus interest, was transferred out of the Interest  
4 Income Fund, and gets distributed into the RJRT Common Stock  
5 Fund, \$3,763, as well as the two Vanguard Funds, 11,200 in  
6 each of them.

7 If you combine the information from all three  
8 subaccounts which have NGH money, and you can see the total  
9 amount of NGH money that ended up in the RJRT Fund, and  
10 that's \$870 for the basic pretax on the first page, plus  
11 3,278 for the basic after tax, which to keep a running total  
12 is about \$4,100, and then you have another \$3,763 in the  
13 company cash match, which gets you up above \$8,000 that can  
14 be traced from the NGH Common Stock Fund into the RJRT Fund,  
15 so you have on the order of \$8,000 or so.

16 I can see -- according to Mr. Altman, I see  
17 \$7,912, so maybe my math in my head wasn't exactly right,  
18 but it's approximately correct. So it is not true that as  
19 Mr. Altman claims, that only \$1,500 worth of NGH Funds could  
20 be traced into RJRT. It is in fact a much larger number.

21 BY MR. CHARNES:

22 Q. Doctor Montgomery, I would like to shift gears a little  
23 bit and return to your basic data calculations and move away  
24 from Mr. Altman.

25 Did you make any -- after conducting your two

1 approaches; most similar and tracing method, did you make  
2 any adjustments to your damages analysis based on the  
3 certain legal defenses asserted by Defendant?

4 A. Yes, I did.

5 Q. What were those?

6 A. Well, there were two adjustments related to excluding  
7 portions of the class from damages. The first of those  
8 adjustments excluded from the damages calculations  
9 participants who signed a release after liquidating their  
10 entire NGH and NA investment within the Plan.

11 The second exclusion was to exclude individual  
12 participants who liquidated their entire NGH and NA holdings  
13 within the Plan, before those holdings were forcibly  
14 liquidated on January 31st, 2000. I considered damages  
15 excluding either alternatively, each of those two groups and  
16 then excluding both groups combined.

17 MR. LEWIS: Can we have a standing objection to  
18 the testimony about both of those exclusions, given the  
19 legal issues?

20 THE COURT: Certainly you may.

21 BY MR. CHARNES:

22 Q. Obviously, Doctor Montgomery, you aren't taking any  
23 position whether the legal exclusions are correct or not?

24 A. That's correct, I'm not taking any position.

25 Q. Would you please turn to Defendant's Exhibit 266.

1           THE COURT: Does that conclude the Plaintiff's  
2 volume 11?

3           MR. CHARNES: I believe so, Your Honor.

4 BY MR. CHARNES:

5 Q. Let me know when you're there, Doctor Montgomery.

6 A. I'm there.

7 Q. What is Defendant's 266?

8 A. This is a list of early liquidators in the class, and  
9 this was based on our analysis of the participant data that  
10 we received.

11 Q. So you created Defendant's Exhibit 266?

12 A. Yes. My staff did.

13 Q. How did you create it?

14 A. We analyzed each participant's transactions within the  
15 Plan and identified those participants that had completely  
16 liquidated their holdings of NGH and NA before January 31st,  
17 2000.

18 Q. And what does Defendant's Exhibit 266 show?

19 A. It is the name of each of these participants and it  
20 shows that there are 894 participants in the class that  
21 liquidated early.

22 Q. And does this exhibit also contain a redaction for the  
23 social security numbers of the participants?

24 A. Yes, it does.

25 Q. If you please turn to Defendant's Exhibit 71A, which is



1 in binder two. I apologize, Your Honor.

2 A. Okay.

3

4 Q. What is this document?

5 A. This document is a list of class members who signed a  
6 release, according to the list of release signers that we  
7 were provided, who signed a release after liquidating their  
8 entire holdings in NGH and NA.

9 Q. How did NERA create Defendant's Exhibit 71A?

10 A. We received from counsel, and I understand counsel  
11 received these lists from the Defendant, we received lists  
12 of individuals who had signed releases, along with the dates  
13 that they signed the releases, and then these -- we received  
14 several supplements of these lists over time and we compared  
15 the name and social security numbers on those lists to the  
16 Plan records that we received, and we identified the  
17 individuals on the lists of release signers that we received  
18 that were also members of the class, and this is the  
19 basis -- well -- and then we also identified for those  
20 members those individuals who signed the release after fully  
21 liquidating their NGH and NA Holdings. That's the way the  
22 list was constructed.

23 Q. Did you testify earlier, that this list of participants  
24 who signed releases was current through November 30, 2009?

25 A. Yes, I did. It is current through November 30, 2009.

1 Q. Are the list of early sellers and list of releasors  
2 mutually exclusive?

3 A. No, they are not.

4 Q. So participant class members could be on both lists?

5 A. That's correct. There is some overlap.

6 Q. If you please turn back to Defendant's Exhibit 244,  
7 which is in notebook four. What is this document?

8 A. This document is an exhibit that summarizes my estimate  
9 of alleged damages under the tracing method based on the  
10 full appreciation of NGH and NA following January 31st, 2000  
11 through December 11, 2000.

12 Q. These are damages as of December 11, 2000?

13 A. That is correct.

14 Q. And does Defendant's Exhibit 244 accurately represent  
15 your calculations applying that method?

16 A. Yes, it does.

17 Q. Would you please explain to the Court the result of  
18 your calculations using the tracing method.

19 A. The exhibit shows four options, option one through  
20 option four, and these options relate to which of the two  
21 previous groups; early liquidators or releasors is excluded  
22 from the damages calculation. The first option excludes  
23 neither group, that is to say it includes all class members  
24 in the damages. There are 3,287 class members with positive  
25 damages. I should say, there are another roughly 300 class

1 members who have negative damages, and they are excluded  
2 from this calculation. The 3,287 class members had total  
3 aggregate damages of approximately \$27.7 million as of  
4 December 11, 2000.

5 The next option is option two, and that shows damages  
6 removing releasors, the number of individuals who signed a  
7 release after fully liquidating their NA and NGH Holdings  
8 and having -- have to have positive damages was 1,088, and  
9 if these individuals are excluded, the overall damages is  
10 just a little under \$18.0 million.

11 Option three excludes -- includes release signers, but  
12 excludes all early sellers, all early liquidators of NGH or  
13 NA, and if the 653 individuals with positive damages and who  
14 are early liquidators are excluded, damages are  
15 approximately \$20.3 million.

16 Finally, option four excludes both groups, both  
17 releasors and early sellers. This results in the exclusion  
18 of 1,510 class members, and if these individuals are  
19 excluded from damages, damages are approximately  
20 \$13.5 million.

21 Q. Doctor Montgomery, can you please explain for the Court  
22 how a class member could have negative damages.

23 A. A class member would have negative damages, if the  
24 class member basically was better off having -- it would  
25 have been better off -- was better off in the alternative

1 investments, than the class members would have been had they  
2 retained NGH or NA until December 11, 2000.

3 An example of how this might come to pass is, a class  
4 member might have liquidated his -- say he had a position in  
5 NGH and he might have liquidated that position early, early  
6 on, say in July of 1999, and perhaps invested in the Total  
7 Stock Market Fund, and so gained the benefit of the  
8 appreciation of the overall stock market in 1999, while NGH  
9 was actually declining in value, and then had the luck or  
10 whatever, to switch out his stocks in early 2000 and either  
11 invest in the Interest Income Fund, or more likely, this  
12 happened in some instances, invest in RJR Tobacco at that  
13 point, and then gain the benefit of RJR Tobacco appreciation  
14 in 2000.

15 So this is an example of somebody who would have  
16 negative damages under the tracing methodology.

17 Q. If you please turn to Defendant's Exhibit 245.

18 A. You said 245?

19 Q. Yes, sir. What is DX 245?

20 MR. LEWIS: Objection, Your Honor.

21 MR. CHARNES: I'm not sure I understand the basis  
22 of the objection.

23 THE COURT: I had sustained the objection to his  
24 being able to state an opinion with regard to what investors  
25 likely would have done.

1 MR. CHARNES: I interpreted your -- maybe  
2 incorrectly -- your standing objection to his comparison as  
3 to which of the two methods he thought was more appropriate.

4 THE COURT: No. I sustained it as to this method.

5 MR. CHARNES: Okay, Your Honor.

6 THE COURT: That's why I was going to give you the  
7 opportunity to follow up on questions, if you had additional  
8 questions to support that method.

9 MR. CHARNES: I apologize. I didn't understand  
10 that. If we could maybe confer for a minute.

11 THE COURT: You may. Sure. You want a five  
12 minute recess?

13 MR. CHARNES: Sure. Thank you, Your Honor.

14 (Recess taken from 5:10 p.m. to 5:15 p.m.)

15 MR. CHARNES: If it is okay with the Court, I  
16 would like to ask a few more questions of Doctor Montgomery  
17 related to the most similar method.

18 THE COURT: All right, sir.

19 BY MR. CHARNES:

20 Q. Could you please again describe for the Court how you  
21 determined what funds available in the Capital Investment  
22 Plan after January 31st, 2000 were most similar to the NGH  
23 and NA Funds.

24 A. Well, in short, I analyzed each fund's returns, the  
25 risk characteristics of each fund's returns and risk

1 characteristic, looked at the volatility of each fund in  
2 comparison to NGH and NA and the correlation of each fund  
3 with NGH and NA.

4 THE COURT: In doing that, did you then assume  
5 that each investor would find the most similar fund to the  
6 Nabisco Stock Fund that investor was in and put the money in  
7 that most similar fund?

8 THE WITNESS: I'm not sure if I assumed it  
9 necessarily. The calculation of damages were compared with  
10 a comparison of what the investor would have received.

11 THE COURT: If they had invested --

12 THE WITNESS: If they had invested in NGH or NA,  
13 that's the hypothetical.

14 THE COURT: What is the basis --

15 THE WITNESS: With the investment that they  
16 actually made, that was closest to NA and NGH in terms of  
17 the risk characteristics. So that's the calculation as  
18 comparison of NGH and NA returns with the investment that  
19 participants actually made closest, similar to NA or NGH in  
20 terms of risk.

21 THE COURT: Okay. Go ahead. I obviously don't  
22 understand.

23 BY MR. CHARNES:

24 Q. Doctor Montgomery, in applying the most similar  
25 investment methodology, did you make any assumptions at all

1 about what participants actually would have invested in but  
2 for the removal of the NGH or NA Funds?

3 A. I think, as I stated, it's -- the calculation compares  
4 the actual returns in NA and NGH to the returns of all the  
5 funds that the participant actually invested in, to ones  
6 that are the most similar based on the risk characteristics  
7 to NGH or NA, and it's either NGH or NA, depending on what  
8 that participant had been investing in, in which stock is  
9 the basis for the damages calculation.

10 THE COURT: And you did that for each participant?

11 THE WITNESS: That's correct.

12 THE COURT: So walk me through a typical  
13 participant.

14 THE WITNESS: All right. So a typical participant  
15 would have had -- the most typical participant is a  
16 participant who had NGH Stock until January 31st, 2000, and  
17 then may have -- and also, after that stock was liquidated  
18 on February 1st, had investments in say, RJ Reynolds  
19 Tobacco, in the Total Stock Market Fund, and so the Interest  
20 Income Fund -- I'm just making up what I think is probably a  
21 fairly typical example, but it's only a hypothetical  
22 example. And the damages calculation would be a comparison  
23 of the hypothetical returns that investor would have  
24 received, had that investor been able to keep -- stay  
25 invested in NGH up until December 11, 2000, in this

1 instance, because that investor had RJR Tobacco Stock and  
2 assuming they had enough RJR Tobacco Stock with the returns  
3 in RJR Tobacco. If that investor didn't have RJR Tobacco  
4 Stock, it would involve a comparison of NGH returns with the  
5 next most similar investment, which in this case would be  
6 the total sock.

7 THE COURT: You're assuming that the investor put  
8 all of his or her money in the most similar fund?

9 THE WITNESS: No. I'm not assuming that. I'm the  
10 investor -- and I'm doing this analysis based on what the  
11 actual -- what the investor actually had. This investor  
12 actually had investments in RJR Tobacco, the Total Stock  
13 Market Fund and the interest income. Those are actual  
14 investments.

15 THE COURT: How about money that was in the  
16 Interest Income Fund, what would you do with that?

17 THE WITNESS: That would not enter into this  
18 particular damages calculation, unless the individual didn't  
19 have an investment that was more similar than the Interest  
20 Income Fund.

21 THE COURT: So if the money from the Nabisco  
22 Stocks was put into the Interest Income Fund --

23 THE WITNESS: Well, that's a -- that's the -- what  
24 you just described there is tracing approach. If the money  
25 is put in -- if that money, if money somehow carries a tag



1 that allows you to identify -- the money didn't really carry  
2 a tag that allows you to identify where it goes, although we  
3 can trace money through the accounts using the methodology I  
4 described, but money is essentially a portfolio, and so the  
5 comparison is not based on trying to see where the NGH money  
6 actually went, that's the tracing methodology. But this  
7 approach doesn't attempt to see where the money actually  
8 went, but rather compares the NGH return with the actual  
9 investment that the participant had that was the most  
10 similar.

11 THE COURT: And what is the basis for doing that?

12 THE WITNESS: The basis is, that there is no -- I  
13 think that the tracing methodology, or any tracing  
14 methodology, assumes that the only thing that would have  
15 changed in a participant's portfolio is the investment that  
16 can actually be traced to the NGH money, and that nothing  
17 else in the participant's portfolio would have changed.  
18 Finance theory says that people manage portfolios as  
19 portfolios, and the most similar method is one way to take  
20 into account risk characteristics that are part of how one  
21 manages a portfolio.

22 THE COURT: Is that consistent with what you  
23 testified to earlier with regard to the participants who had  
24 their money or investments in the Nabisco Funds from June  
25 the 14th until January the 31st of 2000?

1           THE WITNESS: I'm not sure I understand the  
2 question. I'm sorry.

3           THE COURT: Did you not testify earlier today with  
4 regard to the number of participants who did not move their  
5 money at all --

6           THE WITNESS: I see.

7           THE COURT: -- from June the 15th of '99 until  
8 January the 31st of 2000?

9           THE WITNESS: No. I think it is -- it is -- those  
10 participants appeared to be rather passive in their  
11 investments, and I think that my argument there was  
12 essentially that -- a liability argument.

13          THE COURT: What would you do with those investors  
14 with regard to the most similar?

15          THE WITNESS: Well, this is a -- these investors  
16 would be treated the same as other investors.

17          THE COURT: Which is how?

18          THE WITNESS: Which is assuming --

19          THE COURT: Their money is put from the Nabisco  
20 Stocks into the Interest Income Fund, now what do you do  
21 with that?

22          THE WITNESS: It depends on what else they have.

23          THE COURT: If they happen to have some money in  
24 one of the funds that you would consider the most similar,  
25 then you would go to the most similar fund?

1           THE WITNESS: That's correct, because if one takes  
2 the view of liability in this case, that participants were,  
3 you know, actively managing their portfolios and making  
4 choices and were deprived the choices of NA or NGH, it would  
5 make sense to me that they would try to do the best they  
6 could with the choices they had, which would be invest in  
7 the things most similar.

8           THE COURT: Okay. Sustained. That's not coming  
9 in.

10          MR. CHARNES: Thank you.

11          THE COURT: That's not coming in. Now if you  
12 would like to stop here for the day, in view of that and  
13 pick back up tomorrow, we can do that, since we've only got  
14 five more minutes.

15          MR. CHARNES: That will be fine, Your Honor.

16          THE COURT: Let's adjourn until 9:30 in the  
17 morning, unless we have something else we need to talk  
18 about.

19          MR. CHARNES: I'm advised we do, Your Honor.

20          THE COURT: Then, Doctor Montgomery, you can be  
21 excused.

22          MR. CHARNES: I'm advised I misspoke earlier when  
23 I was referring to the compact disk with participant data.  
24 I called them DX 159 and 161. Those are PX numbers. It  
25 is -- I should refer to PX 159 and PX 161, and the correct

1 DX numbers are 205A and 205B.

2 THE COURT: Okay. Hold where you are, if you  
3 would. You had identified them as DX 159 and 161 and they  
4 should be what?

5 MR. CHARNES: PX 159 and 161 or DX 205A and 205B.

6 THE COURT: 205A, 205B?

7 MR. CHARNES: Yes. I apologize for the  
8 misstatement.

9 THE COURT: Thank you. Anything else we should  
10 take up?

11 MR. LEWIS: No, Your Honor.

12 THE COURT: See you all at 9:30 in the morning.

13 (Court adjourned at 5:27 p.m.)  
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## C E R T I F I C A T E

I, J. CALHOUN, RPR, United States District Court  
Reporter for the Middle District of North Carolina, DO HEREBY  
CERTIFY

That the foregoing is a true and correct transcript of  
the proceedings had in the within-entitled action; that I  
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THIS TRANSCRIPT CERTIFICATION IS VOID, IF THE  
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Date: 5-12-10

J. Calhoun, RPR  
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